BUYING (And Keeping) A CAR

From Walking On The Lot
To Driving Away

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Federal Credit Union

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Introduction

Buying a vehicle - whether it's a car, truck, SUV or other set of wheels - can be a remarkably complicated undertaking, with many decision points baked into the process. There's a lot of industry-specific jargon, large numbers and high-pressure sales tactics. There are also a lot of moving parts, which can be overwhelming.



This guide is here to help you navigate the process smoothly. We'll demystify some common car-buying concepts by walking you through the choices step-by-step. By the end of this ebook, you'll know everything you need to know for getting the car of your dreams at a price you can afford.

However, while reading this book is a great start, there's no substitute for in-person advice. Before you step onto the dealer's website or lot, have a talk with someone at the credit union. There are peculiarities to every situation, and you deserve to have someone you trust helping you look at yours. This way, you can go into a dealership forewarned about some of the biggest hurdles you'll face during the car-buying process.

First Steps: New Vs. Used

Maybe it's your first time visiting a car lot as a would-be buyer, and you're beaming with anticipation and nerves while taking this next big step in your life. Maybe it's time you traded in your sports car for a car that's better suited to a growing family. Maybe it's just time to upgrade to something fresh and new. Whatever the case, there's one big question weighing on everyone's mind: Do I buy new or used?

There's no one answer to this question. Much of it depends on your personal situation. Here are a few key factors to help you make up your mind.

1. WARRANTY

First, there's the case of the warranty. Almost all new cars come with a built-in manufacturer's warranty that's good for three years or 60,000 miles. This is an invaluable benefit to buying a new car, as even the best-engineered machines sometimes break down. In addition to major repairs, some warranties cover routine maintenance, such as oil changes. If you have someone else covering the expenses for the first three years, that could be money you're saving. You'll want to make sure you stay on schedule for that routine maintenance, though, or you could invalidate your warranty.

Since the warranty applies for three years, you can sometimes find recently used cars that still have the original manufacturer's warranty. If you buy a used car more than three years after it was produced, that warranty will be gone, so you'll be on your own for mechanical issues that may arise.

2. REPAIRS

Vehicle repairs come with the territory of car ownership, whether you're buying new or used. No matter how well the car is made, some parts will wear out over time. While you can expect to pay more to maintain a used car than a new one, no one gets away completely free. For example, Kelley Blue Book estimates that, in the second year of owning a Honda Accord EX,

drivers may have to spend as much as $1,838 in repairs and maintenance. Those costs typically plateau as the vehicle gets older, but they never go away.

Given the possible expenses involved in repairs, buying a pre-owned vehicle can be a bit of a gamble. Of course, if you're buying from a lot that's connected to a trusted car dealer, it's a pretty safe bet. Many lots inspect incoming cars and perform any necessary repairs or polishing. You'll have to pay a little more at first, but the extra costs will buy you the security of a car without major problems.

Typically, a dealership that also sells new cars will spend the time and money to ensure its used inventory is also up to snuff. Buying from a used car specialist or looking for a vehicle on a site like Craigslist can be a bit more risky. It's definitely cheaper, but you're going into that deal with no idea what the past owner has done to the car. The risks could include anything from a terrible smell to that dreaded check engine light. Whatever it is, you're either going to have to live with it or pay to fix it out of your own pocket.



3. DEPRECIATION

Depreciation is a big concern when buying a vehicle. Depreciation is an asset's loss of value over time. For all the reasons we've talked about and others, a car is worth less the longer it's out of the factory. The biggest depreciation occurs immediately. Any car depreciates by approximately 11% of its original value as soon as it leaves the lot for the first time.

For example, a 2017 Toyota Prius V new costs $26,675. It would depreciate by $2,934 as soon as it rolls off the lot. That's $2,934 you'll never see again, and that's only on the first day. Within the first two years, provided you've kept the car in near-perfect shape, the car will be worth just 74% of its initial purchase price. So that same Prius V would now be worth only $19,739 - meaning you've lost $6,936.

Before buying new, be sure you're ready to make that hefty commitment.

If you're buying used, the loss that new car buyers experience is your gain. For starters, all that money now gone to the depreciation is money you save. If you just wait on buying that Prius V until 2019, you'll be able to buy it for only 74% of what it was originally worth. Not to mention that after the 26% a car loses in the first two years, the amount lost in depreciation drops significantly every year. After the third year, you'd lose only 7% of the original value. After that, the value lost to depreciation is just about negligible. That means that not only do you save more than 25% when you first buy, you also don't need to worry as much about losing money to depreciation. The money's already been lost by someone else; it's not your problem!

Everyone buys cars for different reasons. That means that what they're looking for in a car is different, too, as are the reasons they're willing to save or spend money. Everyone has a different reason to decide whether to buy new or used. But if your goal going in is to save as much money as possible, there are some definite things you'll want to keep in mind.

- *Am I willing to take the risk on the car surpassing its warranty?*
- *Am I willing to pay extra for maintenance and repairs?*
- *Do I want to take a chance that the past owner treated the car poorly?*
- *Is it really worth losing so much money to depreciation?*

The more questions you ask, the more confident you can be in your decision

to buy new or used.

Whether you choose to go new or used, you've only just begun making decisions. Your biggest choice comes in deciding what kind of car to get. This is probably the biggest purchase you'll make other than your home, so you'll want to be confident in your decision. If you're stuck, consider the following:

1. RESALE

How long do you plan to keep your car? Do you plan to drive it until the wheels fall off, or do you see yourself wanting to upgrade in a few years? If this is a car you plan to own for less than five years, you need to look at the potential resale value.

Cars from luxury brands, such as Lexus and Acura, tend to hold their value fairly well. Cars with a reputation for longevity and dependability, like Toyota and Subaru, also tend to depreciate slower than other brands. Also, look for relatively recent vehicle lines. These are car models that will likely still be in production several years from now, ensuring parts and service won't be hard to come by.

2. DAY-TO-DAY

Many people start car shopping by making a list of things they occasionally do or want to do someday. They may want to own a boat, so they need a car that can tow. They go camping sometimes, so a car that can offroad is preferred. This is a good way to end up with more car than you need.

Instead, look at what you use your car for on a daily basis. For most people, this is a commute to work and back. For this, you need a comfortable car that gets good gas mileage and is easy to park. For special occasions, you can always rent a car or truck. How many times a year do you see yourself

picking up furniture or hauling a trailer? If it's less than five, remember that you can still rent a truck or van for such occasions.

3. BUYING OR LEASING?

You have options when it comes to how to purchase your car. You can buy it, which means you'll take out a loan for the purchase price. When the loan is paid off, the car is yours, free and clear. You can also lease a car, which is essentially a long-term rental. At the end of the lease term, you may have the option to buy the car, depending on the terms of the lease. If you choose not to purchase it, you may be charged penalties for things like mileage or damage to the vehicle. If you wreck the car, the insurance company will make the deal whole before they concern themselves with your damages.

Generally speaking, leasing a car isn't as good a deal as buying. If you absolutely must have a top-end luxury car, a lease is one way to make it affordable. The tradeoff, though, is that you are building no equity. You'll never be able to get a trade-in, and you may have to make expensive penalty payments when getting your next car.

FINANCING TIPS AND TRICKS:



After you've picked out your car, your next step will be with the "F&I" department: Financing and Insurance. This is the last opportunity dealers use to make more money off their sale to you. If you're not careful, F & I can stand for fleecing and infuriating! Here's how to get out with the best deal you can.

1. A LITTLE BACKGROUND OF THE INNER WORKINGS OF F&I

Very few dealerships do their own financing. Generally speaking, F&I people take the estimated price of the car, the actual value of the car and your credit history and shop the deal to a number of different financiers, such as banks and credit unions. These include major national lenders, manufacturer financial departments and, depending on the dealership, some local lending institutions. These vendors each quote an interest rate and relevant fee information to the salesperson or sales manager.

Car dealers usually have long-standing business relationships with these lenders, which may include incentives for selling a loan from a specific lender. Because the lenders are competing for the dealer's business, not necessarily for yours, those incentives are for dealers, and not for consumers. While the dealer knows that lower interest rates make you more likely to buy a car, in this transaction, you're not the customer. You're the product. The dealer is trying to sell your business to a lending organization while making as much profit as possible on the transaction.

It may be convenient to handle the financing of your vehicle with the dealer once you've agreed to a sale. However, because of the background detailed above, you can see how you may end up paying a premium for that convenience. Come talk with us at the credit union before you reach that point. We can help you identify price ranges and terms that are best suited to your budget while also getting you pre-approved. It will shorten the process for you, give you buying leverage and minimize your susceptibility to aggressive sales tactics.

2. TAKE THEM FOR A RIDE!

Make no mistake, financing is profitable for dealerships in many ways. If they know they can't turn a profit from financing, they're more likely to push harder to find profit elsewhere. Unless you come in armed with a pre-approval, you're almost always better off if you make financing the last



part of your transaction with the dealership. This doesn't mean, though, that you don't want to think about financing until that point. Discuss your plans with a representative at the credit union, including the type of vehicle you're thinking of buying. Figure out what kind of rates they can offer. By doing your research ahead of time and knowing what financing options are available to you, you can let the dealer think there's still money to be made in the financing, which may strengthen your negotiating position on other parts of the transaction, like the price of the car or the value of the trade-in.

3. DON'T PITY THE SALESPERSON

Most of the time, your salesperson only benefits from the price of the car, the warranty and some high-markup items, like undercarriage treatment and upgrades. The financing department representative, the one responsible for getting quotes and delivering them to the salesperson, is the most likely recipient of any kind of commission on the financing. In these instances, it's also very likely that the salesperson with whom you're dealing has little or no control over your financing. He or she might be able to go back to the financing department and ask them to attempt to negotiate a better rate,

but this negotiation may not have much success. In any case, someone at the dealership profits from getting you a loan, and it's not necessarily you.

4. MIND THE GAP

"GAP," or Guaranteed Asset Protection insurance, is automobile insurance that covers the difference between the total amount of the loan and the value of the car. It's protection against the worst-case scenario, that your car is totaled and you owe more than it is worth. Your comprehensive insurance coverage will only pay out the value of the car, leaving you on the hook for the remaining interest and finance charges. A dealer may require that you purchase GAP insurance as a condition of financing your car. The cost of the insurance is almost always paid up front as part of the financing charges.

GAP insurance is designed for long-term, high-interest or low down payment financing. If you are buying a car without putting a lot of money



down, or if your credit history is not stellar, consider getting GAP insurance. But, as with any other purchase, shop around. Because most financing arrangements require GAP insurance, dealerships maintain institutional arrangements with insurance agencies, expecting you to purchase it without much thought. It's one of the last chances they have to seek profit on the sale, and they rely on you not to notice. You may be able to find better rates on GAP insurance (and other insurances like Mechanical Breakdown coverage and loan Payment Protection) from a broker or from another lending institution.

While you might not think so at first, the credit union offers this type of coverage and has a strong track record of protecting members' purchases. Over the years, we have saved members thousands of dollars on their claims and helped keep debt scenarios from turning into nightmares.

5. STAY STRONG TO THE END

Financing is among the easiest places for dealers to make money because it's almost always the last stop in the car-buying process. They are counting on you to be both committed to purchasing a car and exhausted from making a series of decisions. High-pressure salespeople use this fact to their advantage.

When it comes time to talk financing, frequently the license plates are off your old car and you're sitting down with a sales manager. While it may seem counter-intuitive, this is the best time to walk away and get a second opinion. See if your credit union can offer you a better rate, lower fees or a more flexible term. Ask them to commit, as much as possible, to a price on an offer sheet, then tell them you'd like to take some time to think about it. If you come back with a cashier's check in hand, the sales manager may hem and haw, but at the end of the day they'd rather make the sale than make a little extra on financing.

This is an especially important step if your history with credit is complicated. A giant lending corporation won't see the steps you've taken to solidify your financial position. They don't have the same relationship with you that your credit union does. They see you as a risk number and an interest rate they can justify. Always give your credit union a chance to beat the dealer's offer - your credit union works for you, not for a commission.

Is Zero Percent Financing Worth It?

If you're shopping for a car because you've seen an advertisement for 0% financing, you're not alone. Campaigns like Toyota's "Toyotathon," in which manufacturers offer deals like 0% financing for 60 months, are incredibly popular for car buyers and dealers alike. If it were honestly a losing proposition for the manufacturer, they likely wouldn't keep doing it. How, then, could they possibly make money on the financing? The answer is two-fold: volume and selectivity.

The volume part of the money-making strategy is simple. Zero percent financing gets people on the lot and encourages them to think about buying a specific brand of car. The manufacturer and the dealer both make some



money on each car sold, so the 0% financing trades some profit per car in the hopes that they'll make up for it in number of cars sold.

Selectivity is the other side of volume. Not everyone who comes to a 0% financing event will qualify for that rate. Because most people who get to the point of discussing financing have decided to purchase a car, they'll settle for a non-zero rate. Between these two strategies, advertising 0% financing does pretty well for a car dealer. Car commercials don't talk about the fine print, but dealers put a pile of restrictions on 0% financing. If your history with credit is anything less than perfect, don't expect to qualify for these rates. Roughly 60% of people who apply for these loans end up being rejected.

Also, these loans are usually short-term. If the dealer is offering 0% financing over the life of the loan, expect it to be no more than three years. This means a much higher payment than you'd have on a five- or seven-year loan. Additionally, many 0% financing offers only cover part of the life of the loan - usually six months. After that, you'll be paying more in interest.

Dealers may use the promise of 0% financing to trick you into paying more for the car. With their knowledge of your financing options, they can manipulate the price of your trade-in and the cost of the transaction to arrive at a monthly payment you're happy about. That way, you'll focus on the cost of the payment and not the price of the car or the total amount you'll ultimately pay.

Choosing 0% financing will usually prevent you from taking advantage of other discount options. It is offered instead of manufacturer rebates and other discounts. Also, these financing packages are usually incompatible with special discount programs like Ford's Friends and Family package.

This last hiccup can mean 0% financing is actually more expensive than a loan that's obtained through a private lender like the credit union. To see this effect, let's take a look at some numbers. We'll assume that you're paying $20,000 for a car. You're presented with two choices:

1. You can take 0% financing on a three-year loan.
2. You can get a 4% interest rate on a five-year loan from the credit union, plus a $2,000 manufacturer's rebate.

Let's see how those options break down.

If you take the 0% financing option, your monthly payment will be $555. Assuming no other fees or problems, you'll pay $20,000 over the life of the loan. Your payments will be higher, and if you can't make one of them, you'll be paying more in interest next month (in addition to all the months that follow).
If you take the rebate, though, your monthly payment will be $331 - a much more reasonable amount. Over the life of the loan, you'll pay a total of $19,890. That means you will save $20 and have a lower car payment, too.

Even if it's not compatible with cash back incentives and other rebates, arranging outside funding before you go to the dealership can be a tremendous negotiating advantage. By continually postponing questions of financing, you can let the dealer think there's still money to be made. This position might lead them to give you more on your trade-in, lower the price of the car or offer you more options.



The loan you get to pay for your car may be the biggest financial decision you make outside your home. You owe it to yourself to do your research and treat this decision with diligence. You wouldn't buy a car just because it had an enticing price tag. Why would you do that with a loan?

Remember, dealers make most of their money from financing. They want you to finance your car through their channels because it's one more way for them to profit on the sale. It's also one more piece of information they can use to manipulate the total price of the car in their favor. You can take that power away from them by doing your own research and making your own decision.

The Last Decision: Extended Warranties

You've finally done it!

You've gone through the test drives, the sales talk, the self-doubt and the sleepless nights - plus the mountains of paperwork. But you did it. The car of your dreams is yours. It's yours and it'll be perfect forever.

"But what if it's not?" asks the small voice in your head, echoing the salesman who's sitting across from you. "What if it's not perfect forever? What if something terrible happens to it? You don't want to be the one to pay for that, do you?"

You don't, so you fork over another small mountain of paperwork and another thousand dollars. You are now the proud owner of one of the car industry's biggest cash vacuums: the extended warranty.

The concept of an extended warranty is simple. You give the insurance agency a loan of roughly a thousand dollars, and they'll cover any injuries your car sustains for the next few years. You're supposed to be getting the better end of the deal. They'll tell you that accidents are frequent and expensive, so paying only a thousand dollars is actually saving you money. In reality, more than 55% of participants in a recent consumer report said that they never used the extended warranty they had bought. For those who had been given reason to use it, the cost of the repairs averaged $837, leaving them with a sizable net loss.

As with anything else, there are a few legitimate reasons to invest in an extended warranty. For one, if you're buying a used car, you might want to

use the money you save on the actual car to pay for some extra insurance. Used cars are twice as likely to malfunction as new ones, especially since you don't know how well the past owner treated them. It's also a better idea to insure cars that have more of a history of expensive maintenance - BMWs, Chryslers, Dodges. On car brands that tend to be more reliable - Hondas, Subarus and Toyotas - you can give the warranty a skip.

If you do decide to buy an extended warranty, there are two key questions you should ask yourself. First, are you getting the best deal you can? One-third of the people surveyed reported attempting to negotiate the price down and saved $235 on average. Also, you might think it's a better deal to buy your warranty with your car, but almost all cars come with three years of manufacturer's warranty. Don't pay for something you're already getting



for free. Read every line of the contract to make sure you're getting your money's worth.

Second, are you sure you're not being scammed? Extended warranty scams are easy to pull off. Any low-life who knows how to put a logo at the top of a letter can send you a message from your "insurance provider" in the mail. The letter informs you that your warranty has expired and you need to buy it again. You send them a check. A foot-thick already-signed contract comes back. Then, the minute you find yourself in trouble, they're nowhere to be found.

The best method of defense against a scam like this is to do your research. Call your insurance provider to verify that the offer is real. While you're at it, you can double-check that your warranty hasn't ended. Then, find out when it will, so the next time you get a letter like that you can shred or trash it without any worries.

More than half the time, buying an extended warranty means throwing your cash away. Major breakdowns happen far less often than you'd think, and minor accidents usually cost less than the price of the warranty. If you want the extra security and breathing room that comes with the extended warranty, it may be worthwhile in a few instances. Just always remember to make sure you're not spending more money than you need to, and verify you're not paying for something you could get for free.

Most important, double check everything by calling your insurance provider and reading all the fine print. You may be able to come out of this actually having saved money on an extended warranty.

Car buying budget worksheet

Use this worksheet to record information from your salesperson. Once you arrive at final numbers with the dealer, bring a signed document with the price of the car to the credit union, and let us get you financed!

_____ Maximum Monthly Payment

_____ Cash Down
+
_____ Value of Trade-in
=
_____ Total Down Payment

_____ Price of the Car
-
_____ Total Down Payment
=
_____ Total Financed

Notes