

# Getting good deals on wheels

Believe it or not, people are still buying cars in the current financial pinch. Some are downscaling to cheaper or older vehicles because their existing payments are too high, and others are taking advantage of the many discount deals on offer because sales are slow. But before you rush out to look for new wheels, put the brakes on and follow some practical advice so you don't get taken for a ride ...

**T**hinking of buying a car but can't afford to pay cash? You're not alone. Very few people can find the cash these days to buy a car. In fact, most people find that it's difficult enough scraping together enough cash for the deposit.

You will probably find that after financing your home, financing your car is the second biggest financial borrowing decision you will make. Typically, car finance is over six years (though it is to your advantage to finance over a shorter period), and if you don't make the correct decisions up front, the long-term financial stress far outweighs any joy you may gain from your new set of wheels.

So, what should you look out for before signing the contract and receiving your new set of car keys from a very happy car salesperson? I would suggest that you ask yourself the following five key financial questions before placing your signature on the dotted line:

1. What type of car do I *need* (not what type of car do I *want*)?
2. What monthly repayments can I afford?
3. Have I budgeted for running costs, such as petrol, oil, maintenance and insurance?
4. Do I understand the implications of the balloon payment or residual amount in the contract?
5. Have I negotiated the best deal possible?

## 1. What type of car do I need?

One of the most common mistakes car buyers make is to buy a car that they *want*, instead of the car they *need*. You may *want* the fuel injected, 16-valve sports edition with mag wheels, leather interior and metallic paint finish, but perhaps all you *need* is a safe, reliable car to get you around.

The difference could run into tens of thousands of rands in the cost price and double that after you have paid interest, fees, maintenance and insurance.

This may sound very boring and not at all 'cool', but rather buy a car you need and that you can afford, than buy a car you want and end up finding yourself having to sacrifice basic household living expenses just so you don't fall behind in the monthly repayments.

I suggest you make a list of 'must haves' and 'nice to haves' before you buy your car, and use this checklist when making your final decision. If you find yourself buying a car with more 'nice to haves' than 'must haves', and you are stretching your budget, then it's time to be honest with yourself!

## 2. What monthly repayments can I afford?

It is a sad reality that the average South African is paying 16% of their after-tax income on car repayments – when the recommended threshold is 10%. On average, a balanced budget would have:

- 35% of after-tax income spent on household expenses (groceries, school fees, transport, entertainment, etc);
- 25% spent on financial items (retirement funding, insurance, life assurance, medical aid etc);
- 35% spent on debt repayments (bond and car); and



- 5% put away for savings or debt reduction.
- If you want to live with a balanced budget and you are paying 25% of your after-tax income on bond repayments or rent, then you shouldn't pay more than 10% towards other debt, such as car repayments.

The tables below illustrate the after-tax salary required to repay a loan, assuming you stick to the guideline of not paying more than 10% of your salary towards car repayments.

From the tables below, you can see that for a R75 000 loan over six years it will cost you

### How to save money on car repayments

Repayment over six years at 13% nacm*	After-tax salary (if repayment is 10% of salary)	Loan amount	Total cost of interest
R1 000	R10 000	R50 000	R22 000
R1 250	R12 500	R62 000	R28 000
R1 500	R15 000	R75 000	R33 000
R1 750	R17 500	R87 000	R39 000
R2 000	R20 000	R100 000	R44 000

Of course, if you would prefer to pay the car off over a shorter term (say four years) and pay less interest, this is a great idea, and the table would look like this:

Repayment over four years at 13% nacm*	After-tax salary (if repayment is 10% of salary)	Loan amount	Total cost of interest
R1 000	R10 000	R37 000	R11 000
R1 250	R12 500	R47 000	R13 000
R1 500	R15 000	R56 000	R16 000
R1 750	R17 500	R65 000	R19 000
R2 000	R20 000	R75 000	R21 000

By paying a car off in two thirds of the time, you will save half the interest costs. Such a saving is really worth considering.

\* nacm – nominal annual compounded monthly. This is the nominal interest rate. The effective rate will be higher.

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R33 000 in interest, and over four years the R75 000 loan will cost you R21 000 in interest (a saving of R12 000!).

So, to answer the question 'How much can I afford on car repayments?' I would suggest you try to limit your monthly repayments to no more than 10% of your household income and you also try not to be tempted into repaying over a period of more than four years.

Once you have worked out your affordability levels, then find the car that fits your budget. Don't buy the car that breaks the budget!

## 3. Have I budgeted for running costs?

Do not underestimate the cost of running your car and the impact this will have on your monthly expenses. When determining whether you can afford the monthly running costs of a car, take into account fuel, oil, servicing, maintenance, tyres, and of course, insurance.

Shop around for insurance to get the best possible deal and make sure that each year when you renew insurance, you have insured for the correct replacement cost and have not over-insured the vehicle.

Be aware that the fuel price can change a great deal from month to month. There is no way of estimating what this will be over the life of your vehicle, but it does make buying a fuel-efficient vehicle more attractive.

## 4. Do I understand balloon payments and residuals?

Some credit grantors will offer to finance the car with a 'balloon payment' (or residual payment) at the end of the finance contract. This final payment is typically 40% of the initial cost of the car. This residual is usually what the car is worth when the contract is finalised.

The advantage of financing with a residual is that the amount that needs to be financed is reduced, which makes the monthly payments

more affordable. For example, the car costs R125 000, but the dealer will finance it with a 40% residual or balloon payment. That means that you only have to finance R75 000, and that 40% of R125 000 (R50 000) is due at the end of the finance period.

The disadvantage of this is that after you have finished paying all your monthly instalments, you still owe R50 000, and if you don't have the cash to pay R50 000, you will have to sell the car and hope that you get enough cash from the sale to settle the residual.

If possible, avoid the temptation of financing with a residual. If you can finance the entire purchase price, then once you have finished paying your monthly instalments, you own the car and are now driving a fully paid-for car. It is often said that the best car is a fully paid-for car.

## 5. Have I negotiated the best deal possible?

Never forget that it is your money that you are using to buy the vehicle and that you are in control of your money. Once you have negotiated the best possible price for the car, don't let the car salesman or car finance manager convince you to pay more than a fair amount of interest and other finance charges.

When negotiating the interest rate, you should be aware of your own credit rating and negotiate the best possible rate if you have a clean credit record. You can get your free credit report from [www.experian.co.za](http://www.experian.co.za) or [www.transunion.co.za](http://www.transunion.co.za).

The days of 'prime less 2%' are a distant memory, and with the credit crunch at the moment, most car finance starts at 'prime plus 2%'. At the time of writing, the prime interest rate was 11%. Bear in mind that if you manage to negotiate a rate of 12% instead of 13% on a R100 000 car over six years, you will save yourself R3 800 in interest costs.

Credit grantors will also try and charge you the maximum fees allowed by the National Credit Regulator. They will charge you a once-off R1 140 initiation fee and R57 per month service fee. Neither of these fees are compulsory, and with some tough negotiating you can get them reduced and at best eliminated.

The credit grantor must give you a 'pre-agreement quote' setting out all the terms and conditions of the loan, as well the total cost of credit. By law, this quote is valid for five days.

Use the five days to examine the quote before signing. Also use this period to get other quotes from other banks or credit grantors and try to get better interest rates and fees. Don't make it easy for the credit grantor – it's your money!

So, before you take the major decision to finance a car, ask yourself the above five questions, and then enjoy the ride.

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