Options available when purchasing a vehicle

Few people are able to pay cash for a vehicle outright, which makes it important to understand the options available when deciding to purchase a vehicle.

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Imperial Auto explains the difference between financing a car, and leasing it.

Leasing a vehicle effectively means that you are renting it by paying a monthly fee to use the car. When the lease term is over, you hand the car back to the dealership or you could choose to buy it back at the vehicle's value at that time.

Pros

- The monthly rental is fixed for the full period of the lease, and you won't be affected by interest rate hikes - making it easier for you to budget for the full period of the lease.
- The lease amount is likely to be significantly less than a monthly repayment on a loan would be.
- Your monthly leasing fee usually includes comprehensive insurance.
- Because the vehicle is never actually yours, you're not vulnerable to unexpected loss in value when the time comes to look at a new vehicle.
- Because leasing periods are shorter than conventional finance deals, the vehicle will most likely be covered by any warranties, guarantees, as well as any service or maintenance plans that are sold with the car.
- You'll get to have the thrill of a new car every few years, as you switch over to a new vehicle at the end of every lease term.

Cons

- You will never own a car outright, unless you choose to purchase your vehicle at the end of the lease term.
- If you choose to purchase the car at the end of the lease, you will be paying the market value of the vehicle at that date, with this price not taking into consideration any of the lease payments you have already made. You will most likely have to finance the full purchase price of this now-second-hand car, extending the time that you're paying for the car significantly.
- Many lease agreements place a cap on mileage, so you need to be aware of your average annual mileage before signing the agreement, or you could be penalised.

Vehicle financing

Financing a car means that you will borrow money from a financial institution to purchase the car, agreeing to pay off a certain amount each month, with this amount including interest.

You can also choose to finance the vehicle and include a balloon payment at the end of the deal - which means that you have the flexibility afforded by a lower loan payment, but it also means that you will be liable for a lump sum at the end of the term.

Pros

- Once you have made all the payments, the vehicle is yours.
- Once you have paid the vehicle off, you will have that much extra wiggle room in your monthly budget - although it would be smart to continue to set that money aside every month in a savings account, in preparation for any emergencies.
- If you decide to sell the car once you've owned it outright for a while, you will still realise value in the sale.

Cons

- While your vehicle may initially be covered by a service or motor plan, once these have expired you will have to cover any service, maintenance or repair costs.
- Your car's rate of depreciation may be quicker than the rate at which you pay the loan off. That means that if you want to sell the car before the loan term is up, you may be forced to sell it for less money than you still owe the bank.
- You have no idea what your circumstances will be in a few years' time, so if you opt for a balloon payment at the end of your finance deal, you could be in for some unforeseen monetary juggling - or you may have to refinance the vehicle in order to make the balloon payment, significantly increasing your cost of ownership.
- Unless you pay a premium rate to fix your interest rate, your monthly payments will fluctuate as interest rates fluctuate.
- You will need to shop around for insurance, as financial institutions insist that vehicles purchased with loans are covered.