KEY

Buying or Leasing a Car

Objective

In this lesson, you will

assess important considerations related to buying or leasing a car.

Car Loans and Car Leases

Taking out a loan to buy means borrowing money to pay for the car from a **bank** or financial institution. You repay the loan to the bank in **monthly** installments. If you miss payments, the car will be **repossessed**.

Leasing a car is like **renting** one for a long time. You pay monthly installments to the **car** dealership. At the end of the lease period, you can choose to either **buy** the car for its lower resale value or **return** it to the dealer.

- ○ Buying ◉ Leasing is better for someone who wants to change their car every few years.
- ◉ Buying ○ Leasing is better for someone who likes to keep a car for a long time.
- ◉ Buying ○ Leasing is better for someone who drives more than the average number of miles.
- ○ Buying ◉ Leasing is better for someone who wants lower monthly payments.
- ◉ Buying ○ Leasing is better for someone who prefers having trade-in or resale value.
- ○ Buying ◉ Leasing is better for someone who wants a car that is always under warranty.

Dealer Incentives

Dealer incentives are agreements between a car **manufacturer** and a car **dealer** that lower the price the dealer pays for a car.

Dealers can earn incentives for selling new **models** of cars or not-so-new models.

Basically, the **more** cars the dealers sell, the **more** the car manufacturers reward them, so it's a win-win situation.

Calculating Monthly and Total Costs

To find the cost of buying a car, use the following formulas:

1. $\text{Monthly Cost} = \frac{(\text{price of car} - \text{down payment}) + \text{total interest}}{\text{number of months}}$
2. $\text{Total Interest} = (\underline{\text{price}} \text{ of car} - \text{down payment}) \times \underline{\text{interest}} \text{ rate} \times \frac{\text{number of months}}{12}$

Then calculate the total cost using this formula:

$$\text{Total Cost} = \text{Down Payment} + (\text{Monthly } \underline{\text{Cost}} \times \text{Number of } \underline{\text{Months}})$$

When you lease a car, you may or may not be required to make a **down** payment. Then you pay a certain amount each month with **interest** for the lease period. This amount is calculated on the difference in the actual price of the car and its **depreciated** (or residual) value over the lease period.

1. $\text{Cost for Lease Period} = \text{price of the car} - \underline{\text{residual}} \text{ value}$
2. $\text{Monthly Cost} = \frac{(\text{cost for lease period} - \text{down payment}) + \text{total interest}}{\text{number of months}}$
3. $\text{Total Interest} = (\text{price of } \underline{\text{car}} - \text{down payment}) \times \underline{\text{interest}} \text{ rate} \times \frac{\text{number of months}}{12}$

Use this formula to calculate the total amount you will spend on the car, if you decide to buy the car at the end of the lease:

$$\text{Total Cost} = \text{Down Payment} + (\underline{\text{Monthly}} \text{ Cost} \times \text{Number of Months}) + \underline{\text{Residual}} \text{ Value}$$

If you decide to return the car at the end of the lease, you can calculate the total cost of the car using the following formula:

$$\text{Total Cost} = \text{Down Payment} + (\text{Monthly Cost} \times \text{Number of Months})$$

Mia recently bought a car worth $20,000 on loan with an interest rate of 6.6%. She made a down payment of $1,000 and has to repay the loan within two years (24 months). Calculate her total cost.

- ☐ $22,204
- ☑ $22,508
- ☐ $22,640

Buy vs. Lease

Gina has her mind set on a car worth $20,000. She wants to use the car for 24 months.
If Gina leases the car, its residual value will be $10,000. Her down payment is $500 regardless of whether she leases or buys the car. As a student, Gina wants the lowest monthly payment she can get.

Which choice will be better? ◉ lease ○ buy

Summary

When is a car loan better than a car lease?

Answers will vary.