LEASING VS. BUYING A CAR

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Purchasing a new (or new-to-you) car is an exciting time. First, you choose the right car, truck, or SUV to fit your unique lifestyle. Then, there's the test drive, where you fall in love with your new ride. Afterwards, there's the final step: financing your new vehicle.

The financing portion of buying your next vehicle is certainly necessary. Fortunately, though, dealerships have the connections and knowledge to walk you through this important step.

Generally, there are two choices for financing a new car: leasing or buying. Each has its benefits and drawbacks, and deciding which option is the best for you depends on your finances, lifestyle, driving routine, and preferences.

This buyer's guide compares the pros and cons of buying and leasing, the economics behind each option, and why you might choose to finance one way over the other. Let's dive in and explore the major differences between leasing and buying a car.

Car Buying 101: Understanding Auto Loans

Whether or not paying for your vehicle in full is in your budget, it's more than likely easier to obtain an auto loan to cover the cost of your new car over time.

Here's what you can expect if you choose to use an auto loan to pay for your vehicle:

How Auto Loans Work

Auto loans involve borrowing money from a dealership, bank, credit union, or private lender to pay for the vehicle's value, plus interest, over a given period of time. Lenders look at a combination of your credit score and income to determine the interest rates that drivers qualify for. Then, they generate loan agreements based on that information. Once an agreement is reached, drivers are obligated to make monthly payments during the term of their loan. A loan term typically ranges between three and six years.

Up-Front Costs of Buying a Car

With car loans, most people make a 20% down payment to secure their purchase and reduce the cost of their monthly payments. Other up-front costs for buying a car include registration, taxes, and documentation fees.

Understanding Leases

Leasing was an option once reserved for corporate and luxury car shoppers. Today, leases account for nearly one-third of vehicle sales, and are found at every level of the automotive industry. As the prices of cars continue to rise, leases offer an affordable alternative to auto loans since their monthly payments tend to be less. Here's how they work:

What's a Car Lease?

Leasing a vehicle is slightly different than buying. It involves borrowing a car's value from a dealership, minus the price of a down payment or trade-in.

As with auto loans, an interest rate is added to monthly lease payments, minus the amount paid along the way. However, lease payments are only based on a vehicle's depreciation, or deterioration in value, instead of its overall price. Thus, monthly lease payments tend to be cheaper than auto loans.

Up-Front Costs for Leasing

Generally, drivers cover the down payment, first month's lease payment, taxes, registration, and other fees to secure their lease at a dealership. They'll also make a refundable security deposit.

Differences Between Buying & Leasing

There are some key differences between leases and auto loans you should be aware of. First, **drivers who lease don't own the vehicle**. They'll be required to return their car to the dealership at the end of a lease term, which is usually two to three years, and they'll have the option to purchase it then.

Most leases come with a mileage cap ranging between 12,000 and 15,000 miles per year. Drivers can negotiate a higher mileage limit with their dealership, but can expect charges at the end of their lease if they go above the agreed-upon cap.

Drivers must be vigilant about maintaining their vehicle during the term of their lease. If the vehicle sustained excessive wear and tear while in the driver's possession, the driver will be charged.

Buying vs. Leasing: Benefits & Drawbacks

Whether you choose to buy or lease, each option has its pros and cons. One isn't necessarily better than the other, so you'll need to look at several lifestyle and financial factors to determine what's best for you. To help you pick the most appropriate option, we've broken down the benefits and drawbacks of buying and leasing below.

Benefits of Owning a Car

- Once you've finished paying off a car loan, you own the vehicle in full. Once the loan term ends, the lender will transfer the car's title to you, and you'll no longer have to factor the loan payment into your budget.

- Buying a car is a great option for drivers who keep their vehicles for more than a few years. You can customize and drive it as much as you'd like, and you don't have to worry about selling or trading until you're ready.

- Owning a car is also an opportunity to build equity, if your payments outpace the vehicle's rate of depreciation. This can help pay for your next car.

Benefits of Leasing a Car

- Leasing protects drivers from unexpected depreciation. For example, if a vehicle's value drops due to unexpected circumstances, like recalls or increasing gas prices, this decrease won't hurt the person leasing.

- You pay a smaller sales tax when you lease a vehicle.

- Leasing is also a great option for those who want more car for less money. Let's say you want a luxury sedan for business—perhaps to entertain clients—but the payment on a car loan is too high for your budget. Leasing could be a great way to get the vehicle with the safety features, technology, and luxury amenities you want at a more affordable price.

- Many leases last three years, which is the standard length of a new car warranty. That means that the vehicle is covered under warranty for unforeseen repairs during your lease term.

Drawbacks of Buying a Car

- Generally, drivers are required to make a larger down payment when they buy a car. Many lenders require at least 10% to 20% of the vehicle's value up front, if you take out an auto loan. For example, if you purchase a vehicle that's $40,000, that's between $4,000 and $8,000.

- Additionally, monthly payments on a car loan are usually higher than they'd be for leases since you're paying for the entire value of the vehicle, plus interest, taxes, and fees.

Drawbacks of Leasing a Car

- Many drivers who terminate their lease early will be penalized. If your driving needs change during your lease period and you end your agreement early, you'll be charged.

- Leases include strict mileage restrictions. If violated, drivers could be subjected to a penalty. Before leasing, estimate the average number of miles you put on a vehicle each year. It may be more appropriate to buy a car if you have a long commute, live in a rural area, or frequently take road trips.

- The vehicle must be returned to the dealership in a sellable condition at the end of a lease term. Otherwise, you could be charged for excessive wear and tear. Read the terms and conditions of your lease contract carefully to find out what's allowed.

- When you lease a car, you're renting it for a short period of time and financing the part of its life your lease covers. That means you won't have equity in the car or anything to trade in when your lease ends. If you want to buy the car once the lease is up, you'll be required to take out a loan with a higher interest rate to pay for the rest of its value.

Leasing vs. Buying: Which Option Is Best for Me?

There's no one-size-fits-all approach to leasing or buying a vehicle. Before choosing your next vehicle, you need to think carefully about the pros and cons of each, and decide which is a better fit for your situation. Here are some questions to ask yourself before deciding to buy or lease a car:

- On average, how many miles do I put on my car each year?

- Instead of leasing a luxury vehicle, would it make more sense to buy a used one of similar quality?

- Do I plan on driving this car for a long time, or will I want a new one in a few years?

- What size down payment can I afford to make?
- After factoring in gas, insurance, maintenance, and the cost of ownership, what's my monthly budget for a car payment?
- If I lease a vehicle, will I be able to keep up with regularly scheduled maintenance and repairs?
- Will my driving needs change over the next three to five years?

If you're not sure whether buying or leasing a vehicle is right for you, contact the car dealership that has the model you're interested in. They can help find a payment plan that makes sense for your driving preferences, lifestyle, and financial background, and will answer any questions you have about the differences between buying vs. leasing a vehicle.

Happy car shopping!

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