

Buying a Car

“Getting Around Town”

Life Smarts:

- Determine the affordability of purchasing and owning a vehicle.

Costs of owning a car

There are many factors to consider when owning a car. Gas prices take a huge chunk of a driver’s budget on a weekly basis. According to AAA, the average driver spends about \$8,776 per year (based on 15,000 miles of annual driving). Insurance is another expense of owning a car. To purchase a car, you will probably need to get a loan. Most car loans last three to six years, and if you miss your monthly payments, you run the risk of having your car repossessed. Regular maintenance is also imperative when owning a car. Items such as oil changes, tire rotations, and tune-ups all add to the longevity of your vehicle; thus, it’s a good idea to have these things done on a routine basis. Finally, you might consider spending money on safety features; items like car alarms, however, add to the cost of the vehicle.

Assuming you own a car, indicate how much you might spend on each of the following items per month.

Answers will vary.

| Gas | Maintenance | Loan payment | Insurance | Safety |
|-----|-------------|--------------|-----------|--------|
| | | | | |

Gas cost comparisons

As mentioned above, gas is a huge expense of operating a vehicle. High gas prices force many people to live close to work and school to save on gas costs. Living near a grocery store or with relatives might also be considerations.

Choosing the right car to fit your needs is very important. When choosing a vehicle, consider how many miles you will be driving and the expected **miles per gallon (MPG)**. To compute the MPG, determine how many gallons are required to fill up at the gas pump. Next, track the number of miles driven and the number of gallons of gas used.

For example, if your car takes 15 gallons of gas and you drive for 350 miles until your tank is empty, your MPG will be computed as follows:

$$350 \text{ miles} / 15 \text{ gallons} = 23.33 \text{ (MPG)}$$

The higher the MPG, the farther you can drive without having to fill up your tank. In essence, you will be able to save money throughout the lifetime of owning the car by putting gas in less often. In some cases, you may be able to save thousands of dollars over several years. The money you save in gas costs can be put toward other investments to help build wealth.

Compute your Miles Per Gallon (MPG):

- You drive to work and school five days per week.
- You fill up your tank with nine gallons of gas and can drive it approximately 380 miles before having to re-fuel.

Answer: $380 / 9 = 42.22$ MPG

Cost of insurance

Another expense of owning a car is car insurance. Like other types of insurance, the process of obtaining car insurance can be complicated because of the different types of coverage. Some key features to consider when purchasing insurance is the amount of the deductible and the type of coverage. Keep in mind that the higher the deductible, the lower the monthly payment will be.

As for types of coverage, the basic coverage needed includes: **Bodily Injury, Property Damage, Liability, Medical Payments, and Uninsured Motorist**. Bear in mind that in New Mexico, as with many states, it is mandatory to have car liability insurance. Call and ask several insurance agents about rates; compare policies to obtain quotes. This will ensure that you receive the best terms and rates for you. Insurance rates for drivers under 25 (particularly males) will be higher, so make sure to ask for possible discounts. Refer to the “Homeowner’s and Auto Insurance” unit for additional information.

Car payment examples

Most people who purchase a car do not have enough money to purchase it without obtaining a loan from a credit union, bank, or other source. Most car loans range between three to five years. This means that if you are approved for a five-year loan, you will make 60 payments, computed as follows:

$$(12 \text{ months per year} \times 5 \text{ years} = 60 \text{ months})$$

This is quite a burden, so it is important to have continuous income in order to make the monthly payment. Keep in mind that by taking out a loan to purchase the car, you will also have to pay interest on the loan. Thus, you will be paying more than the price of the car (principal plus interest).

| Example | 1 | 2 | 3 |
|--------------------------|-----------------|-----------------|-----------------|
| Purchase Price of Car | \$10,000 | \$10,000 | \$10,000 |
| Loan Term in Months | 48 | 60 | 72 |
| Interest Rate | 2% | 2% | 2% |
| Monthly Payment | \$217 | \$176 | \$148 |
| Total Amount Paid | \$10,416 | \$10,560 | \$10,656 |

As you can see from the table, the longer your loan is, the lower your monthly payment, but the more interest you end up paying over the length of the loan. In the example, you end paying \$240 (\$10,416 - \$10,656) more in interest for a 72-month loan vs. a 48-month loan. Thus, when obtaining a loan to purchase a vehicle, you must decide if you want to pay less interest or make a larger monthly payment.

Average cost of maintaining a vehicle

To maintain a vehicle, an owner must pay for fuel, repair, maintenance, and tires. Additional costs include insurance, license and registration fees, taxes, and finance charges. All of these costs must be paid over the life of the vehicle.

According to AAA, the average cost of maintaining a vehicle varies from 45.1 cents to 63.3 cents per mile. For example, if you own a minivan, AAA estimates that on average, it will cost 63.3 cents per mile to maintain. If you drove the minivan 15,000 miles, it will cost (\$0.633 x 15,000 miles) or \$9,485.00 to maintain on a yearly basis. The table below provides estimated costs per mile of maintaining certain types of vehicles.

Data obtained from:

<http://www.newmexico.aaa.com/home/automotive/driving-resources/cost-of-driving.html>

AAA's 'Your Driving Costs' study analyzes the cost to own and operate a vehicle in the U.S. Ownership cost factors include: the cost of insurance, license and registration fees, taxes, depreciation, and finance charges. Operational costs include: fuel, maintenance, and tires.

| Based on driving 15,000 miles a year | Small Sedan | Medium Sedan | Large Sedan | Sedan Average | 4WD SUV | Minivan |
|--------------------------------------|-------------|--------------|-------------|---------------|-------------|------------|
| Cost per mile | 45.1 cents | 57.3 cents | 73.2 cents | 58.5 cents | 74.9 cents | 63.3 cents |
| Cost per year | \$6,758.00 | \$8,588.00 | \$10,092.00 | \$8,776.00 | \$11,329.00 | \$9,489.00 |

Should you buy a new or used car?

There are several decisions to make before buying a car. Should you buy new or used? First, never pay the sticker price for a new car. Most car dealerships are open to negotiation in order to get your business. Remember, you can always tell them you are willing to go elsewhere to find a better price.

Keep in mind when purchasing a new car that it decreases in value immediately upon leaving the lot. For example, a new car purchased for \$21,000 will normally decrease in value anywhere from \$1,000 to \$5,000. If you were to sell the car even a short time later, it would be worth that much less than what you originally paid. You can save lots of money by purchasing a used car. There are many places to find vehicles with less than 12,000 miles that are very close to being new. Do your research, and save yourself thousands of dollars.

Where to find used cars

When looking for a used car, ask family or friends first. They might be willing to sell a car, and you might get an outstanding deal. You can usually find cars for sale around town. Look in the newspaper, on dealership websites, and message boards. Another good source is autotrader.com. Like anything else, taking your time and doing your homework can lead to the purchase of a car that meets your needs while saving money.

Considerations when buying a car

There are two important items to consider when buying a car. First, what kind of car do you want; and secondly, can you afford it? The fancier the car, the more you will pay. Once you determine what kind of car to purchase and you find one you can afford, make sure to inspect the vehicle, preferably with a mechanic. Check under the hood for leaks and connections and underneath the car for rust and/or other possible damage. Check for tire wear and the body of the car for possible repairs. Of course, you should test the lights and electrical devices.

Start the engine and check for smoke out of the tailpipe. Write down the **Vehicle Identification Number (VIN)** located on the dashboard to research the vehicle on the Internet. Test drive the vehicle and check for odd noises, steering control, braking, operation of the transmission, windshield operation, air conditioner, heater, and all of the controls on the panel.

It is also advisable to set your priorities before looking for a car. Check with your credit union or bank for financing the loan. What interest rate will they charge? Will they lend you the money? Always attempt to negotiate the price. If an owner or dealership wants the sale, they may consider lowering the price. It never hurts to attempt to get a better deal.

Resources to help your decision-making when buying a car

www.fueleconomy.gov www.nhtsa.gov www.kbb.com
www.hwysafety.org www.carfax4cu.com www.edmunds.com www.consumerreports.org

Government fuel economy Web resources

www.epa.gov/emisweb is a green vehicle guide that identifies vehicles that are fuel-efficient and have clean running engines.

www.fueleconomy.gov compares the miles-per-gallon ratings of different vehicle models manufactured since the mid-1980s.

www.fueleconomy.gov/feg/savemoney.shtml calculates annual fuel estimates.

Life Smarts: Determine the affordability of purchasing and owning a vehicle.

Assume you have worked at the same job since graduating high school two years ago. You work approximately 25 hours per week and make \$12.50 per hour. You take three weeks off during the year for vacation, and your take home-pay is approximately 80% of your gross wages.

What are your gross wages for the entire year?

Answer: $(25 \text{ hours} \times \$12.50 \times 49 \text{ weeks}) = \$15,312.50$

What will your net wages (take home pay) be for the year?

Answer: $(\$15,312.50 \times .80) = \$12,250.00$

You decide you want to buy a car and have approximately \$1,500 in savings. You meet with a loan officer at your financial institution to determine if you qualify to purchase a car. Based on information about your job, salary, and savings account balance, the loan officer concludes that you are eligible for a \$22,000 loan at 3.2% for five years.

Using the recommended websites, find a car that is equal to or less than \$22,000. Determine how much it will cost to purchase and maintain the vehicle of your choice following the steps below:

Answers will vary.

- a) What is the make and model of the car you chose to buy?
- b) What is the MPG for this vehicle?
- c) What is the monthly payment for this car?
- d) How much will you pay (in total) over the five-year period? Hint: Multiply the monthly payment by 60 months)
- e) Based on the chart in Sections 7 and 8, determine the cost to maintain this vehicle on an annual basis.
- f) Can you afford to purchase this vehicle? Explain why or why not.