Jack Fitzgerald

ON CAR FINANCING

Words of wisdom from Jack Fitzgerald, "Understanding how to finance your vehicle purchase is as important as shopping for the best price!"

Over the past six decades, the landscape of automobile financing has changed dramatically. In the 50's there was only one manufacturer finance company, General Motors' GMAC, and they dominated the automobile industry. Their competitors were forced to rely on independent finance companies, local banks and credit unions to provide financing for dealers and their customers. To put things in perspective, used car loans were once as high as 30% APR and 24 months was the normal loan term. Banks were extremely reluctant to finance used vehicles.

In the 60's both Ford and Chrysler opened their own captive finance companies. These new captives created the necessary competition to lower rates for consumers and dealers.

Today, every major automobile company in America (except GM and Chrysler immediately following their bankruptcies) owns a *captive finance company*, or at least has an affiliation with a national bank or finance company that finances vehicles under its brand name.

Captive finance companies are responsible for facilitating the sale of the parent companies cars and trucks by competing aggressively with local banks, credit unions and other captive finance companies to finance cars for consumers even if the consumer has less than perfect credit. They also assist the parent companies dealers to obtain inventory, real estate, capital loans and other types of financing required to operate the dealership business.

Competing with local banks and credit unions, these captive finance companies have helped create competition that has lowered interest rates for consumers and dealers.

History

1950's

In 1959, the lowest auto loan rate in Washington D. C. was 5% "add-on" (about 10% APR) and FHA loans were 4%. GMAC was the only captive finance company. GM and its dealers were the largest and most financially solid car company.

1960's

In the early 60's both Ford and Chrysler opened their own captive finance companies. These new captives created the necessary competition to lower rates for consumers and dealers.

1970's

In the early 70's import manufacturers found they needed to own their own finance company to be competitive so all of them opened captives i.e. Honda Credit, Toyota Motor Credit, Volkswagen Credit, etc.

Car Dealers vs. Banks

Your car dealer utilizes these captive finance companies to help you finance your vehicle. Car dealers provide all the car loan functions of a branch office of a bank. Captive finance companies rely 100% on dealers who provide the staffing, overhead and other operating expenses so that banks or finance companies do not have to. Dealers earn a commission on the loans they make in order to pay for this overhead for all these duties necessary to complete the transaction.

With the large volume of business a dealer sends to a wide range of lenders, they have an advantage in obtaining financing for high-risk borrowers with credit difficulties. In addition, dealers sometimes provide guarantees to the lender and occasionally indemnify the lender against the loss if the vehicle is repossessed. Not surprisingly, they earn substantial commissions on these transactions.

True captive finance companies create competition for banks and credit unions, which tends to force rates down and provide financing for consumers who have less than perfect credit.

Shop for Financing

So if you are shopping for a car today, keep in mind that you should be shopping both the price and the financing simultaneously instead of separating the two. You will have a better opportunity to make fair comparisons that way because the dealer has a mark-up in both the financing and the car.

But be aware that as some dealers mark-up their cars more than others, some may also mark-up their finance rates more than others. Let your dealer compete on the finance rates just as he does on the price of the car.

Why Your Car Dealer is the Smart Choice

With that said, since your dealer has multiple sources for financing, they will often be your best bet for the lowest financing options available. As a result, you benefit with lower rates, better terms, and more convenience because of the increased competition among all the financing organizations.

Contrary to what has been reported in the news media, consumers DO NOT have to pay any extra for dealer-assisted financing. In fact, dealers borrow money at a wholesale rate not generally available to consumers for financing. So if they choose to, they can provide financing at lower rates.

In my opinion, it is the car dealer who has made the low loan rates of today a reality. If banks really competed on their own, credit card interest rates and other bank charges would be much lower.

So consider placing your loan through a dealer even if your bank can match the rate. It is in your best interest to keep dealers in the finance business because they are the competitive force that has brought car loan rates down and are keeping them low.