Halal Car Finance

u

Halal Car Finance

Before we go into the finer details of obtaining a Halal Car Finance deal let's just begin with the reasons why Car Dealers are so eager to offer finance in the first place. Once you understand this you will also understand how you need to play this out to get what you want from the dealer without getting into a debate or falling out.

How does car finance benefit the dealer?

Although by law a car dealership cannot discriminate between a cash customer and a finance customer in reality they pretty much always do. The law states that regardless of how you pay for your car (cash or finance) the deal offered should be the same to both parties. What actually happens Is that the dealer will push you towards the finance by promising the world and show little interest (excuse the pun) when you say you are paying cash.

The reasons for this are that dealerships are targeted on how many finance deals they do and also receive generous commissions from finance companies for putting the deal their way, especially when charging a higher rate of interest.

I will mention at this stage the difference between APR and flat rate as this sometimes causes some confusion.

The APR is the overall combined rate of interest on the loan taking into account such things as price of car, deposit, fees and type of finance involved. It does not offer a comparison between two loans as you can actually have a higher APR on the same amount borrowed but a lower monthly payment. This may not sound possible but it is just the complicated way APR is worked out.

Ask any bank manager to explain how APR is worked out and they will just look at you lost. The flat rate on the other hand is the actual amount charged per year on the amount borrowed. This can be used as a comparison as it is the rate car dealers use to work out your payments.

When you ask a car dealer what the interest rate is they may try and confuse you by mentioning the flat rate such as ‘It’s only 5 percent’. You thing great, assuming they are talking about the APR whereas the actual APR may be 12% or so.

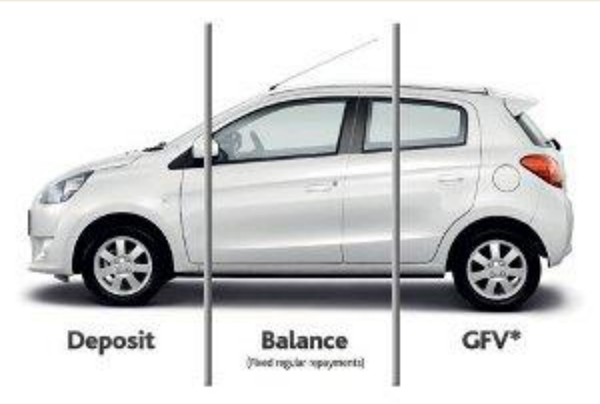
The simplest way to compare two loans is to look at how much you are borrowing and how much you are paying back at the end of it including any fees added.

All dealers will have a base rate of finance set by the finance company and/or by the owners of the dealership. This is simply the lowest rate the dealer can charge without making any finance profit and without incurring any penalty either. Currently this is around 3%-5% for most dealerships.

Let’s assume the base rate is 4%. By charging the customer this rate the dealer earns no finance commission but will earn a fixed amount or percentage amount for simply using the finance company. This is sometimes called Volume Bonus or VB for short. Anything charged over the 4% results in commission plus the VB. Anything charged below the 4% results in a cost but the dealer still gets the VB.

I will come back to these costs later on but first let's just explain the two most popular forms of car finance available:

What is a PCP?



A PCP is a form of car finance similar in principle to a Hire Purchase (HP), but instead of paying off the entire value of the car in monthly instalments, you are effectively only paying off the depreciation.

In other words, you might be borrowing the same amount initially, but you are only repaying a portion of that borrowing. At the end of a PCP agreement, there is still a final value (often known as the balloon or Guaranteed Future Value - *GFV) outstanding. You have several options as to how to deal with this final amount, depending on whether or not you want to keep your car or change it.

What is the attraction of a PCP?

If you compare financing the same car on a PCP against an HP, the big difference is that you are paying off a much smaller amount of money, so you have a lower monthly payment and/or lower initial deposit and/or shorter repayment term.

Most people tend to change their cars about every three years. Most buyers financing a car have a reasonably small deposit. For this sort of situation, a PCP will give a much lower monthly payment than an HP, with the caveat that at the end of the agreement you will have to take action of some sort to settle the outstanding balance. This means that on a PCP, the same car will cost considerably less per month to finance than on an HP, or alternatively you can buy a more expensive car for the same monthly payment. This is what makes a PCP so attractive to the car buyer.

For dealers and manufacturers, a PCP has two great benefits: 1) the lower monthly payments mean that more of their customers can afford more of their cars; and 2) the final balloon payment at the end means that customers will, in all likelihood, buy another car on another PCP, giving the dealer/manufacturer a good opportunity of securing repeat business.

Breaking down the PCP

Deposit

As with an HP, a buyer will put down a deposit on their new car and finance the balance. With a PCP, there is a maximum deposit that is allowed (which varies from finance company to finance company), but usually it's about 30% of the total price of the car. Your deposit can be cash or your current car as part-exchange (trade-in), or a combination of both.

Term

Most PCP deals are available for anywhere between 18 and 48 months, although the most common is 36 months. As a general rule, longer terms give lower monthly payments, although it's not necessarily a dramatic difference because longer terms have lower final balloon payments (which we address below).

Guaranteed Minimum Future Value (the balloon)

The Guaranteed Minimum Future Value (GMFV) is the key to how a PCP works. As mentioned earlier, over the term of your agreement, you are only paying back a portion of the borrowing. When you apply for a PCP, the finance company calculates a predicted minimum value for your car at the end of the agreement, and your deposit and monthly payments are paying off the difference between the initial buying price and this predicted value. This final value then needs to be paid to settle the finance agreement, either by returning the car or paying out the remaining amount.

The finance company guarantees that, subject to certain conditions, that the value of your car at this time will be at least the same as the amount outstanding (hence, a Guaranteed Minimum Future Value). So, if you want, you can simply give the car back to the finance company and the finance is settled. If the market value of the car is less than the amount outstanding, that's not your problem – the finance company takes the loss.

How is the Guaranteed Minimum Future Value calculated?

When you start the finance agreement, the finance company needs to know what the minimum value of the car is likely to be at the end of the agreement. They predict this by taking into account the car you are buying (and some options or features may slightly improve the final value of the car), the length of the agreement (a car will be worth less after 4 years than after 3, for example), and your annual mileage (a car with 60,000 miles on the clock will be worth less than a car with 20,000 miles on it, for example). The finance company will set this future value quite low, as it is their loss if the value drops below what you owe on the car at the end of the agreement. The idea is that the car should be worth a bit more than what is owed at the end of the agreement.

What are my options at the end of the PCP term?

So you have reached the end of your PCP agreement and the finance company has written to you to remind you that you will have to settle the outstanding balance fairly soon. What are your choices? Well, in no particular order:

1) **Give the car back.** The finance company has guaranteed that the value of the car will be equal to the balance outstanding, so you can simply just give it back and walk away.

   This is subject to a few conditions, namely; the car must have not exceeded its agreed mileage, it must have

been serviced on time (and usually by the manufacturer), and there must be no repairs required beyond normal fair wear and tear. If your car does not meet the conditions, there will be financial penalties. Effectively, your PCP has been like a lease.

2) Pay the outstanding balance. Either in cash or by re-financing. You keep your current car and either own it outright or continue to pay off the remaining balance until it is all yours. Effectively, you are turning your PCP into an HP.

2) Part-exchange your car on another one. It doesn't have to be from the same manufacturer or dealer. The dealer when you buy your next car will settle your current finance. If your car is worth more than the GMFV, then any of that extra (called equity) is yours to use as deposit towards your next car.

Say you are offered £12,000 for your car, but your GMFV is £10,000. The dealer will pay £10,000 to settle your finance and the remaining £2,000 is yours to put towards your new car. This is the most common way to settle your PCP, and it is why dealers and manufacturers love it.

You may also be able to sell your car privately and keep any money over and above the GMFV, but check with your finance company first. Some of them are happy with it, but some are not.

Can I settle my PCP early?

Yes you can, but the important thing you need to remember is that the finance company does not guarantee the value of the car against your settlement until the conclusion of the agreement. For example, if you want or need to sell your car two years into a four-year agreement, you will have to pay any difference between what your car is worth and what you still owe (called negative equity). So if your car is worth £20,000 but your finance settlement figure is £22,000, then you will have to pay the extra £2,000 to clear your negative equity.

There is usually a charge to settle a PCP early, but it is not normally large. Some finance companies also allow you to pay in lump sums during the term, to either reduce your monthly payments or bring the end-date forward. Some allow it with no charge, some will charge you for it and some don't allow it at all. Make sure you check before you sign up!

Is a PCP right for me?

You need to make sure you properly understand any finance agreement before you sign up for it. Be aware of exactly how much you are paying in interest and fees, and make sure you are not over-stretching yourself. If that means that you can't afford the car of your dreams, then so be it.

There will always be additional expenses when running a car, and if you can’t afford to eat because your monthly car payment is due then you have made a fairly fundamental error.

Broadly speaking, if you are likely to change your car in a few years’ time, then a PCP can be a cost-effective way to finance it. If you are going to keep it for longer than that, then you may well be better off with an HP and pay the car off in larger equal instalments instead of a few years of lower payments then a big hit at the end.

Read the finance documents carefully and make sure you are comfortable with the numbers offered. Ask as many questions you like before you agree to anything to make sure you understand the full implications of the agreement, as it is better to feel silly before you sign up than feel very stupid afterwards!

Hire Purchase

One of the most common forms of financing a vehicle is through a process known as ‘hire purchase’, which allows you to take ownership of a car once all payments are made. However, how does hire purchase(HP) work and how does it compare to other methods of car finance? This guide to hire purchase will explain.

What is Hire Purchase and how does it work?

Hire purchase combines elements of both a loan and a lease. You reach an agreement with the dealer to pay an initial deposit, typically anything between 10% and 50%, and then pay off the balance in monthly instalments over an agreed period of time. At the end of this period, the car is yours.

Unlike a lease or a personal contract purchase agreement, the residual value of the vehicle is not taken into account. Instead your monthly payments on a hire purchase agreement are determined by the retail price of the vehicle, the size of the deposit and the length of the contract.

In effect, the contract is between you and the lender (usually a bank or broker) but is normally arranged by the dealer. The lender effectively buys the vehicle and allows you to use it while you make payments. Only when all payments are complete is the car officially yours.

What are the pros and cons of Hire Purchase?

The main advantage of a hire purchase agreement is that you can buy something you couldn’t otherwise afford.

Your monthly payments are effectively secured against your car – and this has both pros and cons. Positively, this means you’re more likely to secure finance than you would be by shopping around for an unsecured loan as the lender has some ‘security’ in the form of your car – this is often reflected in better interest rates.

On the downside however, you must be sure you can keep up with payments or the lender will have the right to repossess the vehicle.

Normally this will apply if you've paid less than a third of the agreement – if you've paid more than that it is usually necessary for the bank to take you to court to either reclaim the vehicle or the remaining cash. For most however, this is a safer form of finance than a regular secured loan – which puts your house at jeopardy if you can't meet repayments.

Interest rates can be high – they are usually determined by your credit rating. It's also worth remembering that it's not necessarily in the dealer's interest to get you the best deal – they will encourage you to take hire purchase agreements so they can earn commission from the lender. Their objective is often to sell you money at the highest possible rate – so ask questions and be prepared to look around to other lenders for a better rate of interest.

It's important to check out the Flat rate and total amount to repay to determine what the real cost of borrowing will be. Monthly payments will usually be higher than other forms of car finance, but in the long run the overall sum will usually be lower. It all depends on set up charges and back end fees.

Reselling the vehicle during the hire purchase term can be complicated. You will still need to pay off the money you owe in full. Also watch out for early settlement fees and 'option to purchase' fees. These are not mandatory on hire purchase agreements but will be charged by some dealers.

Who is Hire Purchase right for?

Hire purchase is the traditional form of car finance and is a good way of paying for a car – a sizeable deposit followed by 12 to 60 monthly payments to pay of the rest of the retail price plus any interest.

However, getting a good hire purchase agreement can be difficult – so you must be savvy. Don't just accept the offers that the dealers present to you. Be prepared to ask questions and if necessary, shop around. Remember, the lower the APR, the lower the cash you will have to pay back in the long run. Work out the total amount you will have to repay and always read the small print.

How Does Zero Percent Car Financing Work?

Zero per cent financing is an interest-free loan. However as there is a cost involved to a dealer when offering a zero percent deal this cost has to be outweighed somewhere else.

On used cars the dealers will generally overprice the cars and ask for a big deposit. This then covers any costs involved.

On new cars zero percent is offered on full priced new cars. Once the zero percent deal is over these same cars suddenly offer savings of £3000 or more. What you will never get is zero percent on these cars *and* massive savings.

A buyer who qualifies for zero per cent financing makes a monthly payment that is based on the grand total of the purchase, divided by the term of the loan. For instance, if a car costs £15,600 and the term of the loan is 48 months, then the buyer pays £325 per month.

As is the case with any loan, the buyer must make a monthly payment. In this scenario though, the payment is applied to the principle as no interest is assessed.

Who qualifies for zero per cent financing?

Your credit rating will play a big part in any finance deal zero percent or not. A poor rating may mean that you are not eligible. This is something that neither you nor the dealer has any control over as it is down to the finance companies lending criteria.

So if you are aware that your credit rating is not up to scratch don't push for amazing finance deals as the chances are you won't get them.

So How Do I Get A Zero Percent Deal?

This is actually easier than you may think.

Let's go back to the costs mentioned earlier should the dealer decide to offer a lower rate of finance than the base rate. All finance companies will have a fairly similar structure on this. For example the dealer will be charged an 'x' amount of money per thousand borrowed per rate dropped below the base rate.

As long as you are prepared to cover this cost the dealer has no reason not to set up the whole deal as a zero percent deal. So if for example the cost to the dealer is £1200 they will simply add this on as an 'administration charge' or 'dealer set up fee' and you pay them this as a cash amount.

What they call it will depend on legislation at the time. They may simply refer to it as ‘advance finance charge’. The important thing here is that the dealer cannot offer you this it has to be you, the customer, offering to pay it.

The reason for this is that the dealer can’t charge any fees as such when a zero percent agreement is in place although there is nothing stopping the customer offering a ‘goodwill’ gesture equal to the amount of the zero percent cost.

Incidentally while we are on the subject of zero percent, as I write this I am aware of one finance house who is only charging £30 per thousand pound borrowed per year when setting up a 0% deal. That means you could borrow £10000 over two years at a cost of just £600! (£30 x 10 x 2 years).

The dealer could probably even pay this for you depending on their profit margin.

The rest of the loan is then set up as an interest free amount showing 0% APR.

This does not in any way detract from you negotiating on the price of the car, part exchange or any extra products you may wish to have. In fact seeing as you are technically still a finance customer helping the dealer towards their finance targets and the dealer is still getting their Volume Bonus you may still get a better deal than you expected.

From the dealers point of view they have sold another unit (car), improved their finance penetration and made a little bit of money in the process. It’s what is known as a win:win situation.

This will only work if you go about explaining to the dealership what you intend to do and not demand a zero percent deal or act like a know it all. The ideal thing to do is to make an appointment with the dealership Business/Finance Manager and explain what you are looking to do. He/she will actually help you on this as it is in their interest to get you on board.

Now you may be thinking how is this fair that we have to pay over the car price to receive a 0% deal? Well think about it this way. There is a cost involved to the finance company when lending at zero percent. They are a business not a charity so will never provide any service unless it either benefits them or at least does not cost them.

For comparison let's look at it like this:

You end up taking £5000 on a zero percent deal over four years and it costs you say £1500 in arrangement fees. So in total you will have paid out £6500.

Another customer who has to borrow £5000 and pay interest at 6% per annum will pay back £1200 plus fees of potentially £300 amounting to £6500 in total.

A customer using their savings to pay the £5000 will lose any interest they would receive if they kept their money in the bank for four years. Assuming a savings rate of 5% over four years they will have lost out on just over £1000 in cumulative interest.

Hopefully the above examples will make you realise that you are no better or worse off than anyone else buying a car, which is how it should be.

Real zero percent does not work in the western world. We can only adapt it to suit our Islamic values.

Once again thank you for your kind donation this will help immensely with our forthcoming project 'Halal Income Generator'.

Here we are looking at a fantastic way of setting up your own business, working from home, in your own time if need be and in a totally Islamic compliant way.

We are working with some of the most successful entrepreneurs in the western world to make this possible. These are people just like you and I who started out with very little and have gone onto become millionaires. They have tried and tested proven methods and have now evolved them to benefit the rest of us.

It's not about becoming a millionaire overnight but about setting up a financially secure future for ourselves and our children.

If you thought setting up a business involved a hefty capital or interest bearing bank loans then you are in for a very pleasant surprise.

With our guidance you can now set up a small successful business from your bedroom with only minimal capital. Everything you need to know will be available at your fingertips so let your entrepreneurial imagination run wild.

Just enter your contact details on the Contact Form on www.halalcarfinance.co.uk and we will send you full details once this is up and running.

Wishing you all the best.

Imran Ali Khan

Dr Imran Ali Khan