Types of Finance

Car finance is one of a number of finance options available to fund a car purchase.

The purpose of this information is to give details of the different types of finance you may wish to consider and whether they would be suitable.

The main 5 options are

- Car finance
- Savings
- Personal Loan
- Credit Card
- Mortgage Increase

Car Finance

There are several types of car finance discussed in greater detail on the car finance page. The finance is secured on the car.

Pros: can be cheaper than other options

Cons: you do not own the car until you have repaid the finance in full and may be repossessed if you fail to make your repayments.
There may be limitations within the finance agreement in terms of mileage and wear and tear – these are particularly applicable for PCP where there is an agreed final value.
Usually requires a deposit payment.

Savings

This is the simplest option. Use the money in your bank account to buy a car outright or as a deposit on your car.

Pros: This is usually the cheapest option

Cons: Once you have bought the car, the money is only available to you if you sell the car.

Personal Loan

A loan from your bank or other provider. The finance is not secured on the car. If you fail to make payments on the loan you are personally responsible, your car will not be repossessed without a court order.

Pros: May be a cheaper option.

Cons: May have fewer options than with car finance, for instance the options available with a PCP car loan.
Borrowing amounts and terms with lower interest rates may be limited. Typically small loans and large loans charge higher rates.
No Voluntary Termination option as available with car finance.

Credit Card

If you have a credit card with available balance, you can pay for the car on your credit card.

You need to ensure you can afford the minimum payments on your credit card.

You need to be very confident that you will pay off the balance in reasonable time, otherwise the **interest costs may become very high** and your debt may significantly exceed the value of your car.

This can be a **high risk option** unless you are confident that your total cost of borrowing will be cheapest using this method.

Pros: Maybe a cheap option if you have a low APR on your credit card and will be able to pay down the balance within the low APR period, or your credit rating would mean high borrowing costs on a new finance application.
You get **some protection**. If there is a fault with your car, your credit card is jointly liable with the dealer for correcting it (applies to purchases between £100 and £30,000)

Cons: APR rates are typically quite high on credit cards so **could be expensive**.
High levels of credit card debt may **significantly lower your chances of getting additional credit.** Therefore if you are planning other finance applications eg mortgage or personal loan this may not be suitable. You are also unlikely to get accepted for additional credit cards and therefore it may not be possible to transfer your balance eg after a promotional 0% period has ended.
There is a risk that the debt balance is not paid off in line with the reducing market value of your car, leaving a substantial debt compared with the car value.
The dealer may **charge a fee** for using a credit card.

Mortgage

Depending on your mortgage, you may be able to increase the amount borrowed from your mortgage lender.

Your borrowing is secured on your house. Therefore you must be confident that you will be able to meet the increased mortgage payments, otherwise your house could be at risk of repossession.

This could be **a high risk option** unless you are very confident that:

- your total borrowing costs will be lower,
- you can meet repayments and
- you wish to increase your total mortgage.

Pros: Typically the **interest rates are lower**. You can repay the loan over the remaining life of the mortgage meaning **the repayment amounts may be much lower.**

Cons: Your lender **may not allow** increases and decreases or may charge fees.
The longer you take to repay the finance, the larger the amount of interest you pay. Therefore the **total cost of borrowing may be significantly higher**.

Other Considerations

Finance GAP does not usually cover borrowing for your car purchase with credit card or mortgage

Other Sources of Information

https://www.moneyadviceservice.org.uk/en/articles/whats-the-best-way-to-finance-buying-a-car