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U.S. BUSINESS NEWS

How 0% Financing Deals Destroy Your Car's Value

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There's a little-noted downside to the slew of financing incentives that Detroit is using to keep car sales humming: The enticing deals are triggering sharp declines in the value of cars the minute they drive off the lot.

One reason: Millions of Americans are snapping up new cars, which is increasing the glut of used cars on the market and driving their values down. In addition, the incentives themselves are effectively slashing the prices on new cars, which are a key factor in determining resale values. That also shrinks the value of earlier models already on the road.

MONEY TOOLBOX

Determine whether you should buy or lease, look up a new or used car's True Market Value or find average lending rates in your area in the Money Toolbox[1].

One case in point is the 2000 Ford Taurus SE, which had a sticker price of $19,440 but now is worth only about $8,300.

For shoppers, it's a very good time to buy many kinds of used cars. Many of the best used-car deals are on larger SUVs and smaller cars because they have been so heavily discounted. The typical two-year-old Chevy Suburban C1500, with a $26,421 sticker price, now fetches only $15,404 at trade-in, estimates Edmunds.com, a Santa Monica, Calif., auto-information company. That's $1,400 less than the resale value of the 1998 model at the end of 2000.

LESS THAN ZERO

• GM Resumes 0% Financing In Bid to Pare 2002 Inventory[3]
09/20/02

• Ford Plans 'Free Ride' Offer, With First Payment Due in 2003[4]
09/12/02

• **Eyes on the Road:** Thinking of Buying a New Car? Waiting Might Be the Best Plan[5]
09/09/02

• GM and Ford Are Likely to Raise Prices for Many 2003-Model Cars[6]
07/23/02

COMPANIES

Dow Jones, Reuters

General Motors Corp. (GM)

PRICE	33.64
CHANGE	-2.24
U.S. dollars	11:48 a.m.

Ford Motor Co. (F)

PRICE	7.72
CHANGE	-0.78
U.S. dollars	11:48 a.m.

DaimlerChrysler AG (DCX)

PRICE	31.25
CHANGE	-1.64
U.S. dollars	11:48 a.m.

* At Market Close

The deals aren't as good on popular imports that have relied little, if at all, on discounts to lure customers. A typical two-year-old, six-cylinder 2000 Honda Accord EX sells at trade-in for 39% less than its $24,695 sticker price -- $409 better than the 1998 model bought as a trade-in two years ago.

The financing deals are accelerating the rate at which cars lose their value as they age. It works like this: Buying a $20,000 car with a $2,000 rebate lowers your out-of-pocket cost to $18,000. But the rebate instantly shrinks the new car's value by the same amount. It also lowers the trade-in price of the previous year's model. The effect then cascades through older versions of the vehicle. As a result, a growing number of people trading in used cars owe more on their existing loan than the vehicle is worth.

Resale values also are being hurt by classic supply and demand: Some people who would have bought a used car in the past are now able to afford new vehicles because of the incentives. Also, many people are returning cars as leases expire, worsening the used-auto surplus. As a result, wholesale prices on used cars fell 6.3% in August compared with a year earlier, says Tom Kontos, vice president at car-auctioneer Adesa Corp.

LOSING THEIR VALUE

Here are some of the 2000 model-year vehicles that have suffered from steep depreciation since hitting the road.

MODEL	STICKER PRICE	2000 TRADE-IN VALUE	CURRENT DEPRECIATION
Oldsmobile Silhouette GL	$25,800	$10,462	59.4%
Ford Taurus SE	19,440	8,302	57.3
Chrysler Concorde LX	22,705	9,712	57.2
Dodge Grand Caravan Grand LE	27,950	12,094	56.7
Ford Windstar LX	24,595	10,689	56.5
Chevrolet Blazer LT 4WD	29,120	12,701	56.4
Mazda Millenia S	30,695	13,603	55.7
GMC Sonoma LB	13,505	6,664	50.7
Infiniti QX4 STD 4WD	36,075	20,446	43.3
Nissan Maxima GXE	21,569	11,592	46.3
Chevrolet Suburban C1500	26,421	15,404	41.7

Source: Edmunds.com

And there's no end in sight to the offers causing the sharp price declines. Last week, **General Motors**, **Ford Motor** and **DaimlerChrysler**'s Chrysler unit again extended their interest-free loan offers for many new cars. Incentives from Detroit's Big Three, introduced after last year's terrorist attacks, have kept auto sales strong in an otherwise struggling economy. August was the second-best car-sales month ever, behind last October, when the 0% deals were first introduced.

If your heart is set on a new car, the smartest move could be to pay down existing loans for a year or longer on older vehicles you plan to trade in. And since many models aren't worth as much these days as their owners think, it's increasingly important for buyers to do their homework before kicking any tires, including by using the car-pricing Web sites of the National Automobile Dealers Association, Edmunds.com or Kelley Blue Book.

One model with a bad showing at trade-in time is the Ford Expedition. The sport-utility vehicle's average two-year-old 2000 model has lost 48% of its value -- and is $1,350 worse off than the 1998 model was after being on the road for two years. Ford exacerbated the tumble by throwing in $2,500 rebates or interest-free financing on 2002 models.

In the end, about 85% of the value of all new-car incentives washes through to used-car prices of the same vehicle, says Bob Kurilko, vice president at Edmunds. So if GM puts a $3,000 cash incentive on a vehicle, a year-old car automatically depreciates by $2,550. "It's almost immediate in the marketplace," he says. GM calculates the impact as "somewhere in the 70% range," says Jeff Hichel, the auto maker's director of used-vehicle activities.

Many buyers don't realize how much value their old vehicles have lost until they make a deal on a new car. Jamey Adams, a 32-year-old information-systems consultant who lives in Frederick, Md., last month traded in his two-year-old Ford Explorer toward a new Chrysler Town and Country minivan. He found out that his SUV, with an original sticker price of $28,300, was now worth only $12,000 -- not enough to cover the $15,000 left on his five-year loan. He wound up rolling the leftover $3,000 into his new loan on the minivan.

Consumers owing more on their vehicles than they are worth isn't new -- and is known in the industry as being "upside down." About 40% of buyers trading in their old car a decade ago still owed more on it after the sale, according to CNW Marketing Research, an auto-industry research firm in Bandon, Ore. That percentage sank as the economy soared during the 1990s -- but started to creep up two years ago, reaching 22% through the first seven months of this year. Meanwhile, the size of leftover loan balances rolled into a new loan has ballooned to an average of $2,163 from $617 in 1990.

Auto dealers say the growing number of buyers stuck owing more than their car is worth is linked to incentives that lure customers hooked on new cars back as soon as three months after buying their last car. They are already looking to trade it and get another. "You can't come trade a vehicle in that short a period of time" and expect not to owe anything, says Tracy Schwind, marketing manager at Lujack's Northpark Auto Plaza in Davenport, Iowa. "Zero percent is bringing them into the market sooner."

That's exactly what sent Mr. Adams shopping to replace his two-year-old Explorer. While its plummeting value saddled him with an extra $3,000 on his five-year minivan loan, the fact that he got an interest-free loan made the deal "easier to stomach," he says.

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