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CAR LOAN BY COMMERCIAL BANKS – CONSUMER ATTITUDES' ON SCHEMES

Dr. M. Muthukumar
Assistant Professor, Dept. of Commerce [DDE], Madurai Kamaraj University, Madurai – 625 021.

Abstract

India is considered to be the second fastest growing country in the world. Of late, India has emerged as a pre-dominantly industrialized and service sector focused economy. The growth rate over the last couple of years proved this fact. Liberalization of the economy matched with a young population has led to increase in the incomes and purchasing power. International brands and trends have captured the minds of the young population. Aspiring for better quality products, fast changing life style and higher expectations to grow in life have become the order of the day. A common man, who had a strong aversion to credit, is now in favour of credit for convenience in shopping, for financing housing, automobiles, consumer durables and even to enjoy holidays. The Indian consumer has an opportunity to select from an array of financing schemes offered by a large number of banks and other financial institutions. Commercial banks have now entered into an understanding with non-banking finance companies to meet the growing demands for consumer finance as a result of increased product offering in consumer goods.
Keywords: Liberalization, purchasing power, Commercial banks and non-banking finance.

Introduction

Owning a car is made simple by the fabulous offers of various banks and car finance companies in India. Now-a-days getting an automobile loan is quite easy. Organized and institutional auto mobile finance has come of age and companies aggressively market auto mobile loan schemes by innovative and tempting offers to prospective customers. Most of the lending institutions finance up to 90 per cent of the cost of the car depending on the model of the car and the repayment period.

Trends in Consumer Attitudes

The passenger car industry in India has undergone a drastic change in terms of consumer perception as well as technology. From an extreme perception of cars being an ultimate luxury, today cars have probably acquired the status of an essential utility item to many city dwellers. In 1960's cars were very expensive and only the very rich could afford them. The styles available were limited. During the 1970's a gradual metamorphosis resulted in the perception of viewing cars in the upper middle-class families in India. The 1980's saw the emergence of the "one car for the family" concept. Though the market did not offer much choice, style, orientation and design became desirable attributes in the passenger car. Maruti 800 was launched at a price of just Rs.48,000 in the mid-1980's. At this price many urban based middle class consumers could dream of owning a firsthand car. In July 1991 with the advent of liberalization, restrictions and controls were removed. In particular, the car market experienced the removal of various entry restrictions imposed on foreign companies. Seeing the opportunities the foreign players showed a keen interest in the Indian Market.

Types of Car Buyers

The following are the different types of car buyers.

(i) Imported car buyers.
(ii) Luxury car buyers (Maruti 1000, Standard 2000, Contessa Classic, Premier 118 NE and the like).
(iii) Extended segment (Maruti 800 deluxe).
(iv) Utility car buyers (Maruti 800, Premier Padmini, Fiat, Ambassador).

Market Segmentation

Status Buyers:

(i) The car is bought primarily as a status symbol.
(ii) Brand image associated with the car is very important
(iii) Quality of engineering and attention to finish are very important. In general, looks and styling are important.
(iv) Multiple car owners and light users; usually chauffeur driven.
(v) Economy of operation and cost of maintenance are irrelevant to the purchase decision.

Luxury Car Buyers

(i) The Luxury segment buyers see the car as a measure of upper class living standards.
(ii) Recent entrants rather than higher quality of engineering or brand image tend to be viewed favourbly.
(iii) Emphasis on technology and add-on features.
(iv) Cost of maintenance and economy of operation are not major selling points to this class of buyers. But time loss due to break downs is a major irritant to the buyers in this segment.

Family Car Buyers

(i) Family car buyers prefer comfortable and rather roomy cars.
(ii) Luggage space would be an important criterion.
(iii) Buyers would typically be upper middle class, thus, cost of maintenance would be important.
(iv) Such cars would be used for highway driving.

Upwardly Mobile Professionals

(i) Performance of the car is most important.
(ii) This segment of buyers look for driving ease and operating convenience.
(iii) To a section of such buyers the car is meant to be used as a "stop gap arrangement".

Utility / Functional Buyers

(i) Operating economy, durability, driving ease and ruggedness are desired attributes.
(ii) Wish to have enough facilities in maintaining the car.
(iii) Buyer is price sensitive.
(iv) The car is mainly used for city driving.

Kinds of Car Finance

As compared to the past, getting a car loan is made quick and simple by commercial banks. Some of the popular loan schemes are stated below: An applicant has to select a scheme that is suitable for him/her.

Margin Money Scheme

Under this scheme, customers are required to pay margin money at 10 per cent of the total loan amount, along with one EMI. The balance amount is paid through post-dated cheques; which are issued for the future EMI's covering the remaining period. With a repayment term of one to five years (in some cases seven), the Margin Money Scheme is the most sought after. One of the major advantages of this scheme is that it has the lowest EMI to be paid, as compared to other schemes for the same amount of loan.

Advance Equated Monthly Installment Scheme

This scheme offers 100 per cent of loan amount. Customers have to pay up to five EMIs in advance and the balance is paid through post-dated cheques covering the remaining period of the loan. One of the downsides of this scheme is that though it offers 100 per cent finance, customers need to pay five to nine installments up front. Besides one has to pay a higher EMI amount because the interest is charged on the entire loan amount.

Security Deposit Scheme

Under this scheme applicants are required to deposit a specified sum as security deposit against the amount to be provided as loan. This security deposit is refundable on completion of the full period of the loan. Depositor will receive interest on the deposit, which in most cases is lower than the rate charged on the loan amount. The EMI under this scheme is higher than the EMIs under the above two schemes. The security deposit ranging from 10 - 30 per cent of the total is returned after the loan period. The deposit also earns a simple or compound interest, the tenure lasting for two to five years.

Hire Purchase Schemes

This is an agreement under which the car is let on hire and under which the hirer has an option to purchase the car in accordance with the terms of the agreement. Hire purchase agreement is mostly offered by Non Banking Finance Companies (NBFCs). Broadly this option works similar to the loan option. NBFCs usually charge an amount as low as One Rupee, called Option money, on payment of which the car passes on to the hirer. The NBFCs have taken to this option, as they are not encouraged to give loans, which is a Bank's privilege.

Lease Financing Purchase

Lease is a contract between the owner of an asset (the Lessor) and its user (the Lessee) for the hire of the asset. The ownership rests with the Lessor while the right to use the asset (car) is given to the lessee for an agreed period of time in return for periodic rental payments by the lessee to the lessor. Lease agreements are offered by NBFC's and are mostly availed by corporate looking at it mainly from the tax saving angle.

Tools

Every borrower keeps in mind the Equated Monthly Installments (EMI) fixed for repayment of the loan sanctioned. One makes comparison of EMI of various lenders. Easy finance schemes allow one to walk away with a car, and repay in installments. But choosing the right kinds of car finance is very difficult. The borrowers never know which one is actually beneficial and which one have strings attached to it. A used car, as the customer is not assured of quality, and is not sure of all aspects of the car.

Schemes Available for Car Finance

There are various schemes available for Car Finances at all times. They are stated in brief here.

Margin Money Schemes

Under this scheme if the car costs Rs.1lakh, borrower will have to pay at least 10 per cent upfront with a loan of Rs.90,000. The Loan to Value Ratio (LTV) is 90 per cent. The interest rate will be charged on Rs.90,000. Thus if the rate quoted is 16 per cent for 12 installments; the EMI would be Rs.8, 166.

Security Deposit Schemes

Under this scheme, borrowers can get a 100 per cent loan, but will have to pay 10 per cent of the amount in advance, returnable to the borrower at the end of the loan period. In effect, they still get a loan of 90 per cent. But borrowers are being shown a lower rate because deposit is being used for further loans for the period, when the borrower's money is lying with the company. Some security deposit schemes offer interest also for the deposits.

Hire Purchase and Lease EMI

Equated Monthly Installments and Hire purchase are of the same pattern. The only difference is that under Hire purchase, the size of the installment is known to the hirer and interest is calculated on the loan balance. Under hire purchase, the vehicle is automatically transferred to the buyer as soon as the last installment is paid. Under lease, a separate transaction of buying the lease of car is to be made. Under leasing, the buyer pays a full tax deductible fixed monthly rental. There is no need to separate monthly installments and interest and there is no security deposit.

Advance EMI Schemes

It is another version of the margin money scheme. The bank offers to give the complete amount as loan, but requires the buyers to pay some amount of EMIs in advance. It achieves two things: borrowers make a down payment, thereby reducing the lending amount and the risk along with it. Also, the bank stands to gain on the amount of interest it gets.

Processing Fee

It is the most popular scheme. At the beginning of the period, the bank requires the borrowers to pay 2-4 per cent of the loan amount as processing fee. In effect, the bank is lending less than it had promised that raises the effective rate. For example, if a bank lends Rs.1lakh at 16 per cent for one year (12 EMI) and charges 3 per cent as processing fees, were in effect paying an interest.

DSA/DMA Vs. Dealers

A good bank normally has main Direct Sales Agents (DSA) or Direct Marketing Agents (DMA) under where their operate their subsidiaries. Facilities such as showrooms, or a test drive that are offered by a dealer are not available in case of a direct sale agent, but approaching a DSA has some other advantages. A DSA does processing and such other sundry jobs for which the customer does not have to spend precious time running around. Also, a DSA gives a better deal compared to a dealer. The profile of a customer plays an important role in the whole business. A businessman normally likes to go for a maximum of a 3 year tenure loan because he does not want to be longer around paying interest for a long time. Anyway, he does not want to possess a particular car, especially a small one, for a longer duration. In case of zero per cent interest rate schemes, the EMI is very high and the less the EMI the higher the tenure.

Co applicant

The car finance is taken either in a single name by a individual, or jointly, where there could be more than one person seeking the car finance. If there is more than one person seeking finance, then they are co-applicants.

Guarantor

If the customer's income does not meet the credit criteria, may be asked to have a guarantor for his loan.

Various costs that have to be paid to the finance company to avail of a Car Loan

(i) Interest cost which the finance company charges for providing finance.
(ii) Processing fee: it is a one-time charge taken for processing and legal paperwork. It is in the range of 2-3 per cent of the loan and has to be paid upfront to the company.

Reducing Balance and Flat Rate of Interest

In the 'Flat Rate' system, the rate of interest on the whole amount is calculated over the entire duration of the loan and the principal, plus the interest is divided over the number of installments. But in the 'Reducing Balance' system, also referred to as the Written down Value (WDV) system, the interest is charged on the outstanding balance of the loan.

Security Required Against the Loan

The following are required in a car loan.

(i) Hypothecation of the vehicle.
(ii) Nothing of the hypothecation charge in the books of the RTO.
(iii) Guarantee of spouse, if employed or a third party guarantee, if required.

Tenure of the loan

Tenure is the time-period in which the customer agrees to pay the loan with interest back to the lending bank. In car finance, the choice is the customer's. He can choose from 1-7 years options, depending on his repaying capacity.

EMI

A customer can repay the loan in Equated Monthly Installments (EMI) comprising of principal and the interest. The EMI depends on the quantum of loan, the interest rate and the term of the loan.

Benefits given by the Manufacturers/Dealers

Manufacturing companies or dealers, along with the commercial banks, do bring out schemes from time to time, which give some discount to the customer. The manufacturers/dealers/finance companies may share the discount.

Amount for Registration and Insurance

The amount for registration is 3.5 per cent and 10.5 per cent of the showroom price of the car, for an individual and company, respectively. Insurance is 3.6 per cent of the showroom price of the car for both individuals and companies.

The Conditions in the Financing Agreement between the Individual and the Finance Company

(i) The hirer accepts the entire risk of non-performance; non-delivery, breach or supply of inferior or damaged vehicle by the dealer and the finance company is not liable for the quality, condition or fitness of the vehicle.
(ii) The hirer is entitled to the benefits of the warranties provided by the manufacturer/supplier of the vehicle.
(iii) The hirer shall insure the vehicle and forward the insurance copies to the finance company regularly every year.
(iv) Must pay all duties, taxes and fees or any other outgoing payables in respect of the vehicle and the finance company future in all such payments.
(v) To maintain the vehicle in a good and serviceable order.
(vi) To permit the finance company to inspect the vehicle from time to time. Not to sell, assign, mortgage, encumber or in any other way part with the possession of the vehicle without the permission of the finance company.

State Bank of India (Sbi) - Car Finance

The SBI offers car loans for new and old vehicles and the following are the essential elements in a car loan.

(i) Lowest interest rates.
(ii) Longer repayment period of upto 84 months.
(iii) No hidden costs or administrative charges.
(iv) Finance for one-time road tax, registration fee, insurance premium and accessories.
(v) No advance EMIs.

Eligibility

In order to avail of an SBI Car Loan a borrower must satisfy the following requirements.

i) Age of the individuals ranging from 21 to 65.
ii) A permanent employee of State/Central Government, Public sector Undertaking, private company or a reputed establishment or
iii) A professionals or self-employed individual who is an income tax assessee
iv) A person engaged in agriculture and allied activities.
v) Net Annual Income Rs.100, 000/- and above.

Salient Features

Loan Amount

There is no upper limit for the amount of a car loan. A maximum loan amount of 2.5 times the net annual income can be sanctioned. If married, the borrowers spouse's income could also be considered provided the spouse becomes a co-borrower in the loan. The loan amount includes finance for one-time road tax, registration and insurance. No ceiling on the loan amount for new cars. Loan amount for used cars is subject to a maximum limit of Rs.15 lakh.

Type of Loan

1. Term Loan
2. Overdraft - a) For new vehicles only & b) Minimum loan amount: Rs.3 lacks.

Documents Required

1. Statement of Bank account of the borrower for last the twelve months.
2. Two passport size photographs of borrowers.
3. Signature identification from bankers of borrower(s)
4. A copy of passport/voters ID card/PAN card.
5. Proof of residence.
6. Latest salary-slip showing all deductions
7. I.T. Returns/From 16: Two years for salaried employees and three years for professional/self-employed/businessmen duly accepted by the ITO wherever applicable to be submitted.
8. Proof of official address for non-salaried individuals.
9. A person who is not an account holder of SBI would also need to furnish documents that establish the identity and give proof of residence.

Margin

New/Used vehicles: 15 per cent of the on the road price

Repayment

Repayment period:

For Salaried	:	Maximum of 84 months
For Self-employed & professionals	:	Maximum 60 months
Repayment period for used vehicles	:	upto 84 months from the date of original purchase of the vehicle (subject to maximum tenure as above).

Prepayment Penalty

Prepayment fee of 2 per cent of the amount of the loan prepaid will be levied subject to certain conditions.

Processing Fee

The processing fee is five per cent of the loan amount and to be paid upfront to the Minimum of: Rs.500/ and Maximum of Rs.10, 000.

Banking Activities in the Study Area

The district has a fairly good net work of the commercial bank branches. There are 104 commercial bank branches which operate in the district. Madurai District has a good net work of banks and bank branches. At the time of the study, there were 37 main commercial banks and 104 commercial bank branches in addition to the 47 co-operative bank branches catering to the banking needs of the people in the district. The average population serviced by each bank branch worked out to 10,770 which were much higher than the all India average. The Apex Co-operative Long Term Financing Bank known as the Land Development Bank has been financing long term loans through its net work of 16 Primary Land Development Banks located in different regions throughout the district. The largest branches will found in the State Bank of India and the ICICI bank by public sector and private sector banks respectively followed by the Indian overseas bank, the Indian Bank, the Canara Bank. The least branches were found the central bank of India, the UCO Bank and the State Bank of Travancore.

Conclusion

More than 75 per cent of the total car sales in the study area have been through car loan from commercial banks. Tie-up with dealers and sub-venation money were found to be a major role to promote the sales of passenger car through bank finance. According to dealers, car loan provided by banks can promote the sale and access to purchase by middle class people. The advertisement is the powerful medium to reach the potential buyers about brands of cars. Even a used car can make a severe impression in your bank balance, which is why many people opt to apply for a car loan to pay for their purchase. But quite apart from the fact that car finance enables you to keep your savings where they belong - namely in your pocket.

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