LeasePlan

Company cars: what makes most sense – to lease or to buy?

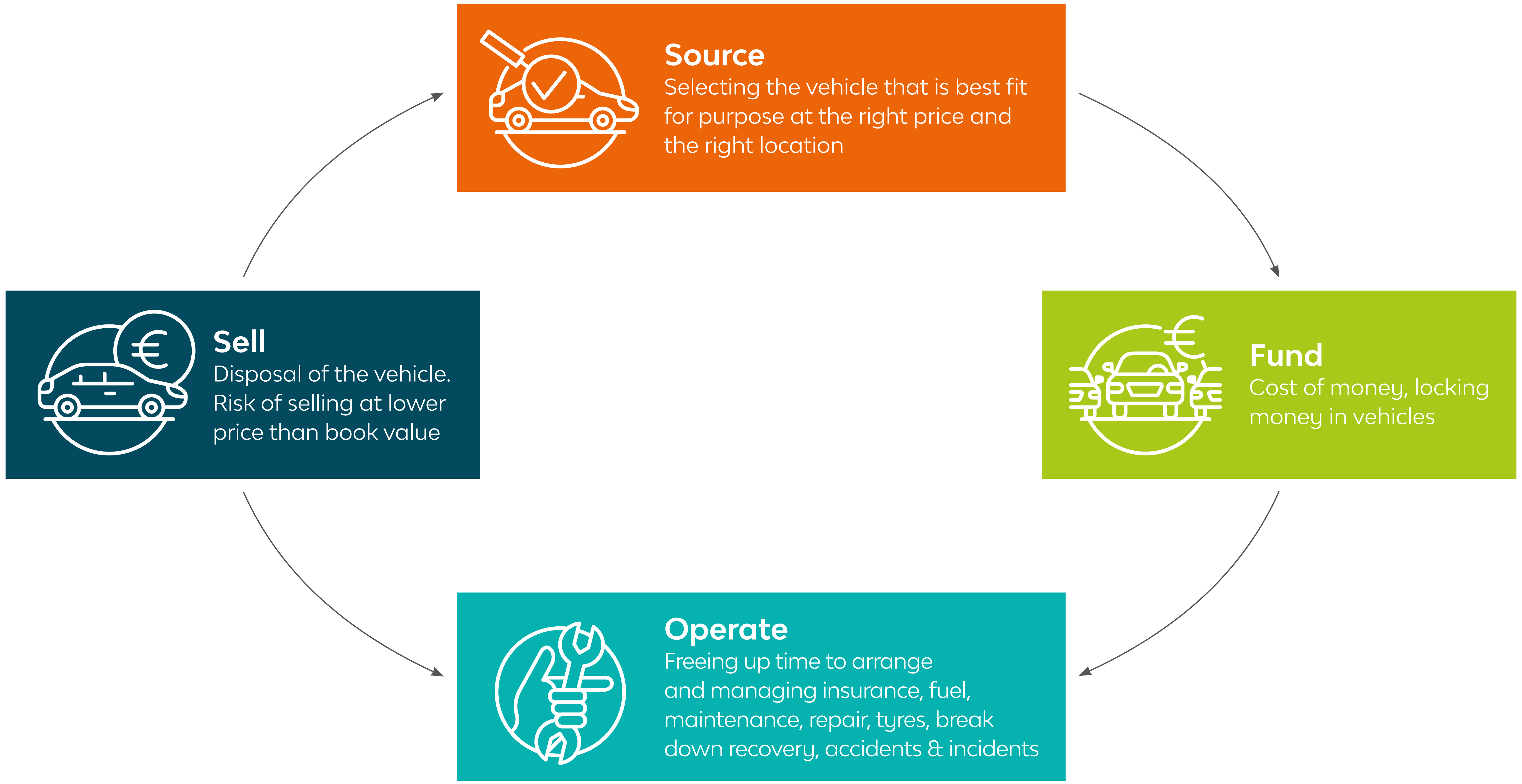
A fresh perspective on both options

What’s next?

When a company requires one or more vehicles to support its business activities, the key question should be: 'What makes the most sense – to lease or to buy?' Small and medium-sized companies (SMEs) in particular often fail to ask themselves this question, either because they just act out of habit or because they believe that their current solution is the best available option. But it is an essential question for every business, as the 'lease versus buy' decision has financial and operational consequences for all types of companies. Leasing is sometimes perceived as an expensive option, but appearances can be deceptive.

A true 'lease versus buy' comparison involves some complex analytical challenges, since the decision impacts not only on the company cash flow, income statement and balance sheet, but also on organisational efficiency in terms of managing the vehicles. Is it perhaps time for you to reassess your stance on leasing versus buying? To help you make the right decision, this white paper compares the advantages and disadvantages of both leasing and buying, highlighting some factors that are often overlooked.

Mobility is an essential business enabler for countless companies nowadays, and they all face the same key decision: whether to buy or lease the vehicles they require. To achieve a fair comparison between leasing and buying, companies should carefully analyse the total cost of ownership (TCO) of both options. Each separate stage of the vehicle life cycle involves different considerations and decisions to be made.



The first step in the vehicle life cycle is to source the vehicle.

Sourcing

Which vehicle is the best fit for your situation and also offers the best value for money? Buying a vehicle rather than leasing it gives you maximum autonomy, flexibility and freedom of choice. You can select whichever vehicle you or your drivers want, request quotes from dealers and place the order with the supplier of your choice. If your company is building a sizeable fleet, it can be possible to negotiate attractive price discounts by using the same local dealership for all purchases based on the promise of future service contracts as well as business/employee referrals.

However, finding the right vehicle for the right price in the right location can be time-consuming and requires a certain level of knowledge and negotiating skills. While leasing can sometimes mean less freedom of choice in terms of vehicle models and dealerships, you always retain ultimate control over the vehicle choice. You not only outsource all the 'hassle', but also benefit from the lease company's expert advice and support in selecting the right vehicle for your situation based on the whole life cost. Moreover, you are assured of the lowest possible price thanks to central sourcing which improves purchasing terms.

Additionally, thanks to their strong relationships with the vehicle suppliers, lease companies have the best access to the newest technologies, enabling you to capitalise on advancements such as improved fuel economy, safety, telematics and suchlike. Even if you require highly specialised vehicles to support your business activities in a specific sector, e.g. construction or food, lease companies can often arrange vehicles that are highly customised in line with your specific technical needs.

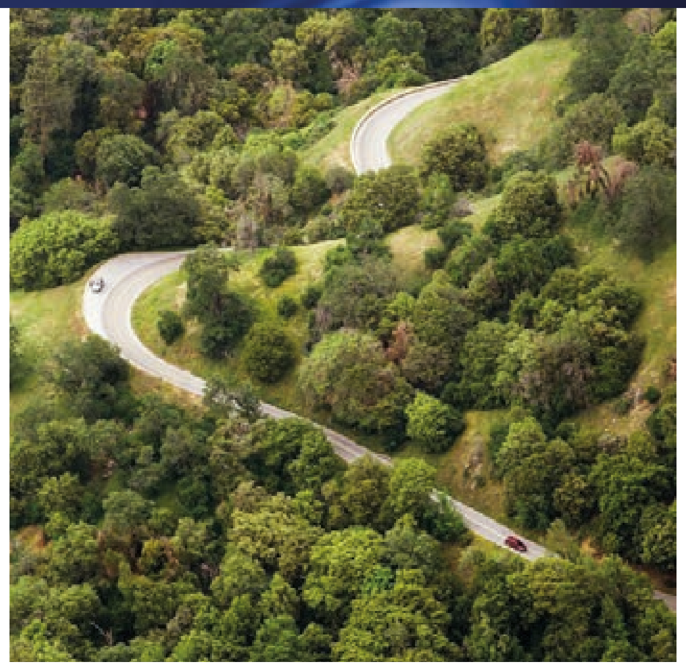
As of 2019, larger companies that report under IFRS and US GAAP lease accounting will be required to recognise a right to use a vehicle and a liability to make lease payments on their balance sheet. Besides this, companies will also see a classification change on their income statement, recognising depreciation and interest for operational leases rather than a lease expense. For further information regarding the upcoming changes in lease accounting, please refer to the LeasePlan white paper on lease accounting. More information on IFRS16 can be found in the News & Media section of our corporate website.

Funding

Once the vehicle has been chosen, the next step is to arrange funding. To make a sound comparison between the 'cost of money' in buying versus leasing scenarios, you need to consider the weighted average cost of capital if you purchase the vehicle against the interest cost that you will be charged in a leasing scenario. Buying one or more vehicles requires you to invest capital in them – tying up money that you could otherwise have spent on your core business. Unless you are a cash-rich company, the money that you lock into your vehicles will come at a cost, either from borrowing or because your investment needs to make a return.

In contrast, leasing enables you to obtain the vehicles you need without using precious operating capital or dipping into credit lines that could be used more beneficially to further build your business. In a lease construction, you pay a fixed monthly fee for the entire lease term to cover depreciation and interest costs based on the vehicle's investment value and its anticipated resale value at the end of the contract. This also supports better forecasting and cash-flow planning thanks to reduced uncertainty and risk.

Last but not least from a funding perspective, there is the issue of warranty. All new cars come with a basic warranty, but it is not always clear what that actually covers. For complete peace of mind it is necessary for owners to purchase an extended warranty, often at considerable expense. In the case of a lease vehicle, even the cost of serious mechanical problems is included in the monthly lease instalment, meaning that the lease company bears the risk rather than exposing you to nasty – and potentially costly – surprises.



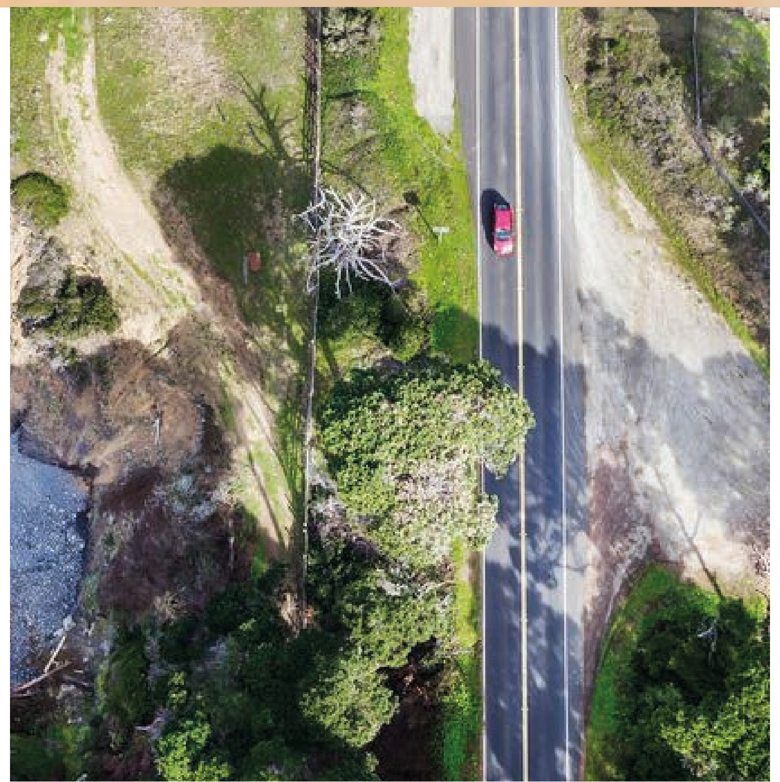
Operational considerations

Once the funding has been arranged, the running costs are the next phase in the vehicle life cycle. Operational considerations include insurance, fuel, maintenance, winter/summer tyre changeovers, breakdown recovery, and the handling of any repairs, accidents and possible claims as well as parking tickets/fines. In a buying scenario you will either have to manage all these yourself in-house – such as by issuing company credit cards or reimbursing employees for fuel costs – or outsource them to a supplier – perhaps your local dealer for maintenance and repairs, and your existing broker in terms of insurance, accident management and claims handling.

However, this aspect of the TCO is often underestimated. Irrespective of the number of vehicles, efficiently managing them involves a considerable amount of work; all these activities require time to find the right supplier, negotiate the right price, to scrutinise incoming invoices and pay them on time, and this can place a significant burden on your fleet manager or administrative department.

In an operational lease setup, the lease company takes care of managing all the operational services, allowing you to focus on your core business. As a guaranteed cost component within the lease agreement, maintenance – including both preventive and unscheduled maintenance as well as roadside repairs – is carried out throughout the vehicle's useful life by an approved supplier, based on service level agreements (SLAs) and approval processes for the work that needs to be done. Tyre changeovers are likewise included in the lease instalment and performed at approved garages with SLAs, and additionally eliminate the problem of storing the spare set of tyres. In terms of fuel, each lease driver receives a fuel card (available in various options) offering good coverage and potential discounts, plus the lease company can provide fuel reports that give you insights into consumption, costs and related CO_2 emissions.

Insurance is another fixed cost component, precisely aligned with the start and end date of the lease contract, as is claims handling, breakdown recovery and accident management (including a replacement vehicle). All of this minimises downtime and offers process efficiency gains for you as a lease customer.



Selling

At the end of the life cycle, once the vehicle has reached a certain age, it needs to be sold or disposed of. This entails a significant risk component for vehicle owners, who have two options: either to depreciate the vehicle to zero and book the sales proceeds as a positive result, or to determine an anticipated resale value and depreciate the vehicle accordingly.

In this case, there is the risk that the vehicle ends up being sold at below the anticipated value, resulting in financial losses. In a closed-end or operating lease agreement, the lease company forecasts the likely residual value at the start of the contract term and calculates your monthly instalments (including depreciation and interest) accordingly. This relieves you of both the worry and the risk of a lower than expected resale value at the end of the lease period.

The advantages of leasing

- You decide on the vehicle specifications and the lease company arranges the rest
- Fixed lease instalment for contract duration; easy to budget and forecast
- Maintenance cost are guaranteed; no unpleasant surprises
- Residual value is guaranteed; no pass-on costs if the vehicle sells at lower price than anticipated
- You benefit from supplier discounts negotiated by the lease company
- You can rely on the vehicle expertise and experience of the lease company
- No hassle; the lease company takes care of arranging and managing all the vehicle-related services and costs.

Conclusion

The lease versus buy decision entails more than just a comparison of the monthly cost of interest/depreciation versus the lease instalment. Every stage of the vehicle life cycle involves considerations that have an impact on the total cost of a vehicle, whether leased or owned, over the course of its useful life. To get a complete picture, in addition to the financial costs on the balance sheet you should also take account of the value of support and handling services provided by a lease company. Such services will reduce the internal workload for fleet managers or administrative employees, and hence ultimately save you extra money.

LeasePlan

LeasePlan Corporation N.V.
Gustav Mahlerlaan 360
1082 ME Amsterdam
The Netherlands
info@leaseplancorp.com

leaseplan.com