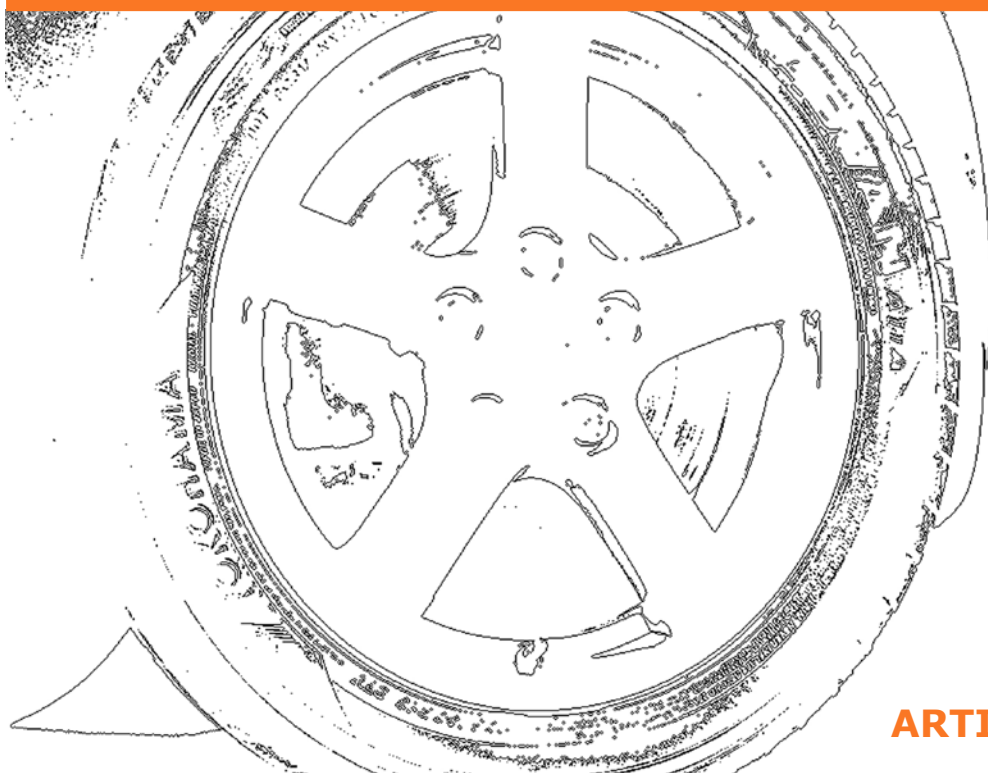


Knowledge

BANK



ARTICLE 39

Personal Contract Hire (PCH)

A guide to personal contract hire (PCH)

Features

Personal contract hire is a consumer product with all of the features and benefits of corporate contract hire.

The underlying contract is a regulated hire agreement (a simple rental or operating lease agreement). The client agrees to pay the rentals for which he or she gets the right to use the vehicle for a period of time. At the end of that period the vehicle is simply handed back to the lessor.

There is no option to own the vehicle at the end of the contract.

As this is a hire agreement the lessor has to charge VAT on the rentals, which most consumers are unable to recover. However, the lessor can recover in full the input VAT paid on the purchase of the vehicle, so this mitigates the effect of the additional VAT the hirer has to pay compared with, for example, PCP. In other words, the hirer has to pay VAT on the rentals under PCH, but the rentals are lower anyway as the leasing company can recover the input VAT on the initial purchase price. The Consumer Credit Act does not require APRs to be quoted on rental-type agreements, so no APRs are quoted on PCH deals.

This can make it slightly harder for a consumer to compare two different rates.

For example, if you are quoted £395 per month on a 3+33 rental profile and another lessor is prepared to supply the vehicle for £400 on a 1+35 basis, which is cheaper? A discounted cash flow exercise would reveal the answer. Here is an example of the discounted cash flow calculation the consumer would have to do, unless they had a financial calculator to hand. How many consumers can do these, particularly while standing in a dealer's showroom?

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A guide to personal contract hire (PCH)

The first table shows the 1+35 rental of £400 per month:

	Opening Balance	Rental	Sub-total	Interest	Closing Balance
1	16,208.50	400.00	15,808.50	131.74	15,940.23
2	15,940.23	400.00	15,540.23	129.50	15,669.74
3	15,669.74	400.00	15,269.74	127.25	15,396.98
4	15,396.98	400.00	14,996.98	124.97	15,121.96
5	15,121.96	400.00	14,721.96	122.68	14,844.64
6	14,844.64	400.00	14,444.64	120.37	14,565.01
7	14,565.01	400.00	14,165.01	118.04	14,283.06
8	14,283.06	400.00	13,883.06	115.69	13,998.75
9	13,998.75	400.00	13,598.75	113.32	13,712.07
10	13,712.07	400.00	13,312.07	110.93	13,423.00
11	13,423.00	400.00	13,023.00	108.53	13,131.53
12	13,131.53	400.00	12,731.53	106.10	12,837.63
13	12,837.63	400.00	12,437.63	103.65	12,541.27
14	12,541.27	400.00	12,141.27	101.18	12,242.45
15	12,242.45	400.00	11,842.45	98.69	11,941.14
16	11,941.14	400.00	11,541.14	96.18	11,637.31
17	11,637.31	400.00	11,237.31	93.64	11,330.96
18	11,330.96	400.00	10,930.96	91.09	11,022.05
19	11,022.05	400.00	10,622.05	88.52	10,710.57
20	10,710.57	400.00	10,310.57	85.92	10,396.49
21	10,396.49	400.00	9,996.49	83.30	10,079.79
22	10,079.79	400.00	9,679.79	80.66	9,760.46
23	9,760.46	400.00	9,360.46	78.00	9,438.46
24	9,438.46	400.00	9,038.46	75.32	9,113.78
25	9,113.78	400.00	8,713.78	72.61	8,786.40
26	8,786.40	400.00	8,386.40	69.89	8,456.28
27	8,456.28	400.00	8,056.28	67.14	8,123.42
28	8,123.42	400.00	7,723.42	64.36	7,787.78
29	7,787.78	400.00	7,387.78	61.56	7,449.34
30	7,449.34	400.00	7,049.34	58.74	7,108.09
31	7,108.09	400.00	6,708.09	55.90	6,763.99
32	6,763.99	400.00	6,363.99	53.03	6,417.02
33	6,417.02	400.00	6,017.02	50.14	6,067.16
34	6,067.16	400.00	5,667.16	47.23	5,714.39
35	5,714.39	400.00	5,314.39	44.29	5,358.68
36	5,358.68	400.00	4,958.68	41.32	5,000.00
		14,400.00		3,191.50	

This shows that the interest rate required to repay £16,208.50 down to a residual value of £5,000 after 36 months with a 1+35 rental pattern is 10% pa.

Example: In month 1, £15,808.50 x 10% divided by 12 = £131.74

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The second table shows the 3+33 rental of £395 per month

	Opening Balance	Rental	Sub-total	Interest	Closing Balance
1	16,208.50	1,185.00	15,023.50	127.13	15,150.62
2	15,150.62	395.00	14,755.62	124.86	14,880.48
3	14,880.48	395.00	14,485.48	122.57	14,608.05
4	14,608.05	395.00	14,213.05	120.27	14,333.32
5	14,333.32	395.00	13,938.32	117.94	14,056.26
6	14,056.26	395.00	13,661.26	115.60	13,776.86
7	13,776.86	395.00	13,381.86	113.23	13,495.10
8	13,495.10	395.00	13,100.10	110.85	13,210.95
9	13,210.95	395.00	12,815.95	108.45	12,924.39
10	12,924.39	395.00	12,529.39	106.02	12,635.41
11	12,635.41	395.00	12,240.41	103.58	12,343.99
12	12,343.99	395.00	11,948.99	101.11	12,050.10
13	12,050.10	395.00	11,655.10	98.62	11,753.72
14	11,753.72	395.00	11,358.72	96.11	11,454.84
15	11,454.84	395.00	11,059.84	93.59	11,153.42
16	11,153.42	395.00	10,758.42	91.04	10,849.46
17	10,849.46	395.00	10,454.46	88.46	10,542.92
18	10,542.92	395.00	10,147.92	85.87	10,233.79
19	10,233.79	395.00	9,838.79	83.25	9,922.04
20	9,922.04	395.00	9,527.04	80.62	9,607.66
21	9,607.66	395.00	9,212.66	77.96	9,290.61
22	9,290.61	395.00	8,895.61	75.27	8,970.89
23	8,970.89	395.00	8,575.89	72.57	8,648.45
24	8,648.45	395.00	8,253.45	69.84	8,323.29
25	8,323.29	395.00	7,928.29	67.09	7,995.38
26	7,995.38	395.00	7,600.38	64.31	7,664.69
27	7,664.69	395.00	7,269.69	61.51	7,331.21
28	7,331.21	395.00	6,936.21	58.69	6,994.90
29	6,994.90	395.00	6,599.90	55.85	6,655.75
30	6,655.75	395.00	6,260.75	52.98	6,313.72
31	6,313.72	395.00	5,918.72	50.08	5,968.81
32	5,968.81	395.00	5,573.81	47.16	5,620.97
33	5,620.97	395.00	5,225.97	44.22	5,270.19
34	5,270.19	395.00	4,875.19	41.25	4,916.44
35	4,916.44	-	4,916.44	41.60	4,958.05
36	4,958.05	-	4,958.05	41.95	5,000.00
		14,220.00		3,011.50	

A guide to personal contract hire (PCH)

The interest rate required to reduce £16,208.50 to a residual value of £5,000 after 36 months, with a 3+33 rental pattern, is 10.154%% pa

Therefore, even though the repayments at £395 per month are £5 lower, the interest rate is higher

This is despite the fact that the total repayments and total interest payable are lower on the 3+33 deal.

Hence the 1+35 deal at £400 per month is cheaper than the 3+33 deal at £395 per month.

Benefits of PCH

The benefit of PCH to the customer is that they simply pay a rental and then hand back the vehicle at the end of the agreement. So long as they do not drive more than the agreed mileage and they hand back the vehicle in reasonable condition, there is no more to pay. PCH is therefore a simple 'pay for use' product.

Disadvantages of PCH

There are few disadvantages to PCH. After all, who can object to paying for the use of a vehicle and handing it back after use? The disadvantages become apparent, however, when comparing PCH to the main alternative, PCP.

PCH offers the customer no opportunity to own the vehicle at the end of the lease. There is no option to purchase. So they can be left with the feeling that they have paid a lot and have nothing to show for it, particularly if they sold their previous vehicle and used the proceeds as the deposit for the PCH deal.

While this is perhaps an irrational customer response – after all, they have got what they paid for – the ability to own the vehicle at the end of the contract is very important for many people.

Historically, demand for PCH has been low, despite a big push by some manufacturers. Demand has risen slightly in recent years but it still seems that in the UK, unlike the USA, consumers prefer to own things rather than to lease them.