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YOUR MONEY

When Is a Lease Not a Lease? When It's an iPhone

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Wealth Matters

By **PAUL SULLIVAN**

APPLE is offering a new way for consumers to purchase iPhones, and while the company is calling the new system a “financing” plan, it is essentially a lease. The idea is to get people to constantly trade in their one- or two-year-old phones for the newest models. And Apple is employing a tactic similar to one that luxury carmakers use to get more people driving Mercedes-Benzes, BMWs, Audis and Lexuses that they could otherwise not afford to buy: creating a monthly payment that is appealingly low.

True, Apple’s plans — starting at \$27 a month to buy a phone over two years, or \$32 a month to upgrade a phone every year — lessen the pain of paying for a \$700 iPhone. Added onto a monthly cellphone bill that probably tops \$100 or \$200 already, the charges may seem slight.

But, of course, these relatively small charges not only accumulate, they never stop, adding one more perpetual charge to consumers’ monthly bills. Why not simply buy something as utilitarian as a smartphone, especially since new iterations offer only incremental changes for the average user? For that matter, why lease a car as

basic as a Chevrolet Malibu — now \$99 a month according to Swapalease.com, an online lease broker — when you could buy a quality used car?

According to consumer experts, economists and analysts, there are both smart and superficial reasons to lease anything.

On the superficial side, a cynic could dismiss leasing a smartphone or a luxury car as just another example of racing to keep up with the Joneses. Some people crave the newest thing. Others judge their self-worth by what they have and how they are perceived by peers.

“Brands are offering this option to consumers who don’t have the lump sum available for the upfront cost,” said Andrea Woroch, a consumer finance and personal savings expert. “But it’s almost about taking advantage of consumers. They can have this fake luxury lifestyle.”

But by now, most people know that. There is also a more concrete reason not to lease something: It costs more over the years of the lease. Ms. Woroch said that if people waited a few months, they could probably buy the newest phone at a lower price, or they could buy a refurbished model of the previous iteration for a few hundred dollars.

The Apple plan also seems more expensive than getting an iPhone through a cellular carrier, which will generally charge a lower down payment and build the rest of the phone’s cost into the monthly payment. Now, someone on the Apple plan could essentially be paying twice — first for the phone, and then for the portion of the phone’s cost that is embedded in a monthly bill.

With cars, which will have a residual value and still be usable after three years in the way a smartphone might not be, the cost of leasing is higher than the cost of financing. But that is where the psychology of leasing comes into play. Car companies make sure that the monthly lease payment is always lower than a monthly financing payment.

That difference is the key to the popularity of leasing luxury cars, said Bob Shullman, founder and chief executive of the Shullman Research Center, which tracks luxury consumer spending. “Leasing cars did not come from the mainstream,” he

said. “It had to do with when you financed a luxury car over the short term, the number was too big. There was a negative backlash.”

In other words, on some level you know that you will eventually pay more later, but focus on the payments that are lower now.

There are upsides to leasing.

Once you own a car, for example, you are responsible not only for maintaining it but also for finding a buyer when you ultimately want to sell it.

“Even if the cost of ownership is lower, the time it takes to resell the car and the uncertainty of what you can get is not worth it for some people,” said Jessie X. Fan, a professor in the family and consumer studies department at the University of Utah who has studied the thinking behind leasing and buying.

“For some people, when these other costs are considered, they will make leasing look better,” she added.

And if that vehicle is leased through a person’s business, the lease payments can be deducted as an expense against income for tax purposes.

Scot Hall, executive vice president of Swapalease.com, said that typically 50 to 80 percent of luxury cars were leased.

Another advantage to leasing is not having to worry that a car may break down or suddenly cost more to maintain.

“The benefit of leasing a car is you get a new version on a schedule, you pay a constant price and, in general today, the lease includes maintenance because the companies realized if they didn’t include maintenance, they get the cars back wrecked after two or three years,” Mr. Shullman said. “Do you get the residual value? No. But it all depends on how important it is for you to have something new.”

Others see advantages to leasing outside of the luxury brands. “All the benefits of leasing a luxury car also apply to your more standard or basic transportation — your Chevys, your Fords, your Toyotas,” Mr. Hall said. “One thing people like about leasing is you can get more car than your monthly payment would typically allow.”

He gave the example of a Honda Accord, which a consumer might be able to afford as a basic model. With a lease, the buyer could upgrade to the top-of-the-line model, with a nicer interior and larger engine. Given that a car loan can now stretch to six or seven years, the three years of a car payment allows the buyer to change cars sooner, he said.

“From the younger generation, they treat their car payment like a cellphone payment — they expect to have car payments and not have it go away,” Mr. Hall said. “It’s a good way for people to budget their money for their transportation needs.”

He said that in addition to the Chevrolet Malibu (\$99 a month), there were 10 other makes leasing for under \$200 a month.

There are other instances in which a leasing model seems to make financial sense. Rent the Runway allows women to lease gowns for special events for 5 to 16 percent of the gown’s value, depending on demand. It has five million members and expects to lease close to \$1 billion in clothing this year.

Our customers “know that when they wear something that is emerald green or burgundy, it’s likely the case that they’ll wear it less frequently,” said Jennifer Hyman, co-founder and chief executive of Rent the Runway. “At least with a black dress or a pair of jeans, you can wear it many times and redecorate it.”

So instead of paying \$6,000 for a gown, she said, someone could rent it for \$600 and get a second size sent along in case the first one did not fit.

The company has another model akin to the original Netflix system of sending users new DVDs after they returned the old ones. For \$99 a month, a woman can have three pieces of clothing and change them out as often as she likes. In this case, the customers are typically choosing clothes for work. (The company does not cater to men, Ms. Hyman said, given their propensity to wear clothes in basic colors for years.)

But back to the Apple plan. While it is certainly to the benefit of the company’s production team to know how many phones will be coming off lease in any given month, consumers also stand to benefit from scheduled upgrades.

This offer “plays into the firm’s strengths,” said Devavrat Debu Purohit, a professor of marketing at Duke’s Fuqua School of Business. “While there is still a market for a three-year-old car or a five-year-old car, a five-year-old phone doesn’t actually work that well. A one-year-old iPhone still works.”

He speaks from experience: When his teenage daughter broke her phone, he gave her an old iPhone 4S he had around the house.

“It’s really frustrating, but it’s not because the phone itself has deteriorated,” he said. “It doesn’t have the memory to work. It’s very slow.”

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