# Auto Loan Rates Could (Finally) Come Down in 2024

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There is a possibility that auto finance rates will start to drop in the next year — here's what that means for car buyers, lenders and the auto industry.

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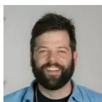
Written by: David Straughan
Senior Writer

Edited by: Rashawn Mitchner
Senior Editor

In August 2023, the average finance rate for a new car loan with a 48-month term reached 8.3% — the highest point since August 2001. Annual percentage rates (APRs) have reached this more-than-two-decade high at the same time as new and used car prices have skyrocketed and rising rates have made cheap car insurance harder to come by, putting substantial strain on car owners around the country.

But after two years of increases, there are strong indications that auto loan rates could start to come back down in 2024 — perhaps by a substantial amount. Such a change could have a considerable impact on individual borrowers and the auto industry at large, just as higher rates have since they began trending upward in early 2022.

## The Federal Funds Rate Could Start To Drop in 2024

In March 2022, the U.S. Federal Reserve (Fed) issued the first in a series of hikes to the federal funds rate, from 0.25% to 0.50%. The federal funds rate is the rate at which the Fed loans money to consumer lending institutions.

The move was the first rate increase since 2018 and was intended to curb runaway inflation, which had reached 6.5% at the time of the decision. Changes to the funds rate tend to correlate directly with rates for consumer lending such as auto loans. Predictably, auto loan

rates began to increase alongside the funds rate. According to data from the Board of Governors of the Federal Reserve System, the average auto loan rate for a 48-month new car loan jumped from 4.87% in January 2022 to 8.30% in September 2023, an increase of 70%.

Both the federal funds rate and the consumer lending rates tied to it have only increased or remained the same since March 2022. But there are indications that this could start to change in 2024.

From the outset, Fed Chairman Jerome Powell has been steadfast about using the funds rate as a tool to slow inflation to a stated target of 2%. The Fed's decision to raise rates has correlated with a significant decrease in the inflation rate, suggesting that its strategy is having the intended effect.

Since the first hike of this latest series, inflation has dropped 38.5%, down to 4% in November 2023, according to the most recent data available from the U.S. Bureau of Labor Statistics (BLS). While this is still short of Powell's target, inflation numbers are headed in the right direction for the Fed to consider an end to rate hikes. That trend has prompted economic policy experts such as James Knightley, chief international economics for ING, to predict that the Fed will start to lower rates as early as the second quarter of 2024.

"We have modest growth and cooling inflation and a cooling labor market — exactly what the Fed wants to see," wrote Knightley in November 2023. "This should confirm no need for any further Fed policy tightening, but the outlook is looking less and less favorable."

In his essay, Knightley said he expects that beginning in the second quarter of 2024, the Fed will begin a series of rate cuts. He predicted that the U.S. will see as many as six 25-basis-point rate cuts — the equivalent of .25% decreases to the funds rate — totaling 150 basis points by the end of the year. If Knightley's prediction holds true, that would put the funds rate at 3.83% before January 2025.

Knightley and ING aren't the only ones expressing optimism about lower rates over the next year. As recently as December 2023, the futures market gave March 2024 rate cuts a 77% probability of occurring. Even Fed officials themselves are predicting lower rates soon, with 17 of 19 projecting that the funds rate will be lower at the end of 2024 than it is now.

## A Rate Decrease Could Help Alleviate Vital Industry Issues

Lower rates would spell relief for cash-strapped Americans in need of financing, but they could also have a pronounced impact on the automotive industry as a whole. The embattled industry has faced a number of substantial issues since the beginning of the COVID-19 pandemic, including supply chain problems, an intensifying affordability crisis and an auto loans industry teetering on disaster.

While they haven't been the only factor, high auto loan rates have played a significant role in exacerbating the affordability crisis and the delicate state of auto financing. Rates have increased at the same time as new and used car prices have gone up, compounding higher prices and adding considerable cost to car purchases. A decrease in the funds rate, and therefore auto loan rates, could help mitigate both issues.

### Lower Rates Would Make Cars More Affordable

While demand is still high for new and used cars, the near future looks somewhat murky for auto sales. A report from Cox Automotive indicated that in December 2023, new vehicle inventories rose to 2.56 million, approaching pre-pandemic levels. This development does give dealerships the ability to offer more choices to buyers, but it could also decrease their profits overall.

Reduced APRs for car buyers would reduce the overall purchase price without cutting down the sticker price of vehicles. As a result, car buyers who may have been waiting for rates to drop may be more motivated to make a purchase.

### Rate Decreases Could Help Avert a Full-Blown Auto Loans Crisis

Lower rates could also reduce the looming threat of serious problems within the auto loans industry. Following the latest series of rate increases, the U.S. has seen delinquency rates rise, the average auto loan payment increase, total auto loan debt surpass student debt and several major institutional lenders exit the auto loans market altogether.

A decision to decrease the funds rate could help stabilize the auto loans market for lending institutions. Lower rates could provide more of a margin for lenders to profit from their auto loans department, for example. Cheaper financing would also likely increase the pool of eligible borrowers as overall purchase prices start to come down.

The current situation is a risky one for lenders, as borrowers have found it increasingly difficult to meet payment obligations. Lower rates would ostensibly provide more affordable financing for borrowers and therefore decrease the risk of missed payments or defaults.

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## Smaller APRs Could Present Opportunities for Car Buyers, Current Borrowers

It's not just lending institutions that could benefit from a decrease to the funds rate, however. Lower rates would also likely help individual borrowers in several ways.

Decreased financing rates would immediately lower the overall cost of new and used vehicles. This would make cars more affordable for buyers — many of whom may currently have difficulty finding desirable vehicles within their budget. It could also potentially make it

easier for car owners to sell their current vehicles, as access to credit loosens and becomes more affordable on the secondary market as well.

Current loan holders would also have an opportunity for some relief if rates go down. People who took out high-interest loans since rate hikes began could refinance their current loans to save money and lessen their monthly payment burden.

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## Lower Auto Loan Rates Could Make 2024 a Good Time To Buy or Refinance

While market predictions are bullish on the funds rate — and by extension, auto loan rates — finally coming back down in 2024, it’s still not a guarantee. Powell and others at the Fed remain committed to their target of 2% inflation. The years since the onset of the COVID-19 pandemic have demonstrated that anything can disrupt business as usual, especially in the automotive industry.

However, with many signs pointing toward lower rates becoming a reality as early as March, it’s not a bad time for buyers and borrowers to prepare for the possibility of cheaper financing. For people waiting for rates to come down to make a purchase, a significant rate drop or series of rate drops could provide an opportunity to move forward with buying a car.

For those holding onto loans with higher rates, 2024 could be a good chance to refinance to lower interest rates and a more affordable loan. However, there are other factors to consider before jumping on a refinancing opportunity. New loans tend to come with additional costs, such as origination fees. Some current loans may also have prepayment penalties that would be triggered when a new loan is used to pay off an existing one. Even with lower rates, refinancing could end up not saving borrowers money or even costing them more overall.

The dramatic increases to auto loan rates since March 2022 have had a substantial impact on the auto industry and individual borrowers. It is reasonable to assume that lower rates would also have sizable effects on both. Without a steadfast guarantee of rate decreases, however, businesses and individuals who may be affected by rate fluctuations would still be wise to prepare for changes to the funds rate — and therefore auto loan rates — in either direction.

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