

Keeping Credit Available and Affordable
Remarks by
NADA Vice Chairman Stephen Wade
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It's a great pleasure to be here with all of you today. I know that many of you are familiar with NADA and our broad range of activities, but for those of you who aren't, let me take a moment to tell you what we do.

NADA is the premier trade association for franchised, new-car dealers. The association was established in 1917, and we serve as the "voice of the dealer" for nearly 18,000 dealers nationwide...large and small, import and domestic. We are the collective face of the dealer to auto manufacturers, the media and the public.

We also offer a wide variety of services and products to help dealers improve their bottom line, and we work to educate dealers about best practices through NADA University, which comprises our 20 Groups, the Dealer Academy and virtual and onsite consulting. Many of the topics we cover are in the all-important financial services area.

One of our most important missions is to represent dealers before Congress and the Administration, and we also focus heavily on helping dealers negotiate the ever-changing regulatory maze that they face on a daily basis. In fact, Andy Koblenz, our vice president of Legal and Regulatory Affairs, is here with me today and will be one of the speakers on the Captive and Independent Lenders panel later this morning.

Today I want to tell you what NADA is doing to keep retail credit available and affordable. As you can imagine, the past two years have been extremely busy for us. We have been working very hard to stabilize the credit markets for dealers, and the status of credit in auto retail and floorplanning.

And we're keeping a sharp eye on the the potential for further regulation of auto financing. Our vigilance paid off around this time last year, when it became clear that the White House was determined to establish a new, far-reaching agency to oversee consumer lending. Most of you are probably well-aware of NADA's opposition throughout the legislative process that resulted in the Consumer Financial Protection Bureau, or CFPB.

The House bill that was originally introduced just about a year ago specifically included new-car dealers under the proposed entity's scope. This was troubling to us for several reasons.

First, it would greatly reduce our ability to provide dealer-assisted financing as a convenient, affordable option for our customers. Consumers win when they have multiple financing sources to choose from. They can always rely on their own banking relationships, but dealers'

relationships with numerous lenders and manufacturers' finance companies allow dealers to arrange financing that regularly meets or beats bank or credit union terms.

Second, while we never welcome new regulations on our businesses, this one was especially onerous and unnecessary. As you know, vehicle loans are already heavily regulated by various government agencies, including the Federal Trade Commission.

And, honestly, it just didn't make sense to include dealers in the new agency's oversight for one simple reason: *the vast majority of dealers don't underwrite, fund or service loans!* We facilitate loans for our customers, and the sources of those loans – banks, credit unions, finance companies – *will be regulated by the CFPB*. Why subject each loan to the same regulatory scrutiny twice? That seems like a waste of time and taxpayers' money, doesn't it?

Add to these reasons the fact that dealers who *do* lend money – so-called buy-here/pay-here dealers – will also be subject to the new regulations, and rightfully so. We never disagreed with that provision.

So, yes, we fought hard to develop *bipartisan* support for the dealers' position. And the House passed a bill that did *not* subject dealers to direct regulation of the CFPB. I'm not going to recount the entire scenario for you – believe me, we don't have time, and I have no desire to relive it – but to say we faced an uphill battle in the Senate doesn't begin to describe it.

But our legislative team visited every Senate office – even those we knew we didn't have a chance of voting our way – and eventually, the facts won out. The Senate voted to support the House's language on dealer financing. That vote, by the way, was 60 to 30 ... it wasn't even close.

The members of the conference committee that reconciled the two bills did, at the eleventh hour, give the FTC expanded authority over dealers. But NADA has a long-standing working relationship with the commission, and we look forward to working with them to further explain the consumer benefits and value of the dealer-assisted financing model.

The new law balances strong consumer protections with affordable access to auto credit. And the bottom line is this: *All vehicle loans will be subject to the oversight of the Consumer Financial Protection Bureau*. Dealers' role in indirect lending will not be subject to the new agency, however. NADA and dealers will work with regulators to structure that oversight in a way that works in the real world.

One aspect that I haven't touched on is the opposition we faced from the Pentagon. Frankly, we were stunned by it. It's not just that dealers are among the most vocal supporters of our troops. Thousands of us employ current or former soldiers and sailors, many of whom have served in Iraq or Afghanistan. In fact, thousands of *us* have served our country in uniform.

Perhaps most puzzling was that we were already working with the Department of Defense to help educate members of the military on the car-buying process and dealer-assisted financing. In fact, it was the cover story in the fall 2007 issue of the magazine *Military Money!* And who

wrote that article? Our own Andy Koblenz, along with AFSA president Chris Steinbert. And NADA will continue to work with DOD to promote financial literacy within the armed forces.

If an army marches on its stomach, the auto industry rolls on credit, plain and simple. And floorplanning credit is no less vital than consumer credit. Both dried up in the wake of the economic collapse.

As you'll recall, in late 2008, the Federal Reserve Board and the Treasury Department established TALF – the Term Asset-Backed Securities Loan Facility – to support the return of consumer lending. From the time TALF opened in March of 2009 until it closed in March of this year, TALF helped bring about \$55 *billion* in auto loans. That covered a full 25 *percent* of auto sales during that twelve-month period!

It took a little longer for us to fully tap into the program for floorplanning credit, but the industry was able to do that in October 2009. Over the next six months, TALF enabled \$9 billion in floorplan securitizations, representing twenty percent of that side of the business. Clearly, TALF was absolutely critical to restoring credit on both sides of the equation, and was an unqualified success.

Oh, and it didn't cost the government a penny.

It's important to understand exactly how dealers survived the economic and industry turmoil of the past eighteen months – and eighty-five percent of us did survive! The reasons for the economic collapse are well-known. The challenges that dealers faced were all as a result of the Wall Street meltdown.

Just as the credit situation began to improve in the spring of 2009, we were hit with the bankruptcy filings of GM and Chrysler. In the midst of the great recession, the forced closing of dealerships added further pain to our industry and to the overall economy and our country. Imagine the thousands of jobs, wages and tax revenue that was lost.

For those of us who were fortunate to continue in business, five major factors contributed to our survival.

First, dealerships that were well-capitalized were in the strongest position to survive. As revenues declined rapidly in all departments, it was critical to have sufficient cash on hand to weather the storm. No one knows better than dealers how important cash reserves are – crisis or no crisis.

Second, expense control was critical. It is never easy to reduce the number of employees we have at our dealerships. But in these challenging times, it became necessary to cut overhead costs, such as personnel and advertising. Just like GM and Chrysler did during the bankruptcy process, we dealers had to establish a “new break-even” for our dealerships. And by doing this, we saved ourselves much-needed capital.

Third, dealers have enjoyed tremendous success in the service and parts departments. Since the late 1980s, we have adopted strategies to leverage these departments. I do not see dealers' dependence on service and parts diminishing anytime soon. In fact, as the market for new vehicles becomes even more competitive, NADA expects that dealers will continue to rely on used vehicles and parts and service to generate revenue.

Fourth, dealers have survived because many of them have a diverse group of franchises. NADA estimates that more than 42 percent of our members have multiple franchises. In difficult times, having multiple franchises is an insurance policy to alleviating the difficulties of a downturn. While no franchise was immune to the challenges, the fact that a dealer owns more than one franchise is critical to weathering any downturn.

Finally, as the recession continued, the Federal Reserve kept interest rates low, and that has had a positive effect on our wholesale credit lines and the capital loans that dealers hold. It is also helping credit-worthy customers secure reasonable rates for financing of their vehicle purchases. For almost 20 years, used-car sales, service and parts have been the profit generators. In 2008, for the first time, the sales in both the new- and used-vehicle departments were in decline. The slight loss in used vehicle sales is attributed to the large swings in the value of used trucks and sport-utilities that year.

Used-vehicle sales were a welcome surprise in 2009; as new-vehicle sales volumes declined, there was a shortage of used vehicles. This simple supply-and-demand problem has led to used-vehicle sales prices being 15 percent to 20 percent higher in 2009. This trend has continued into 2010, although at a slower growth rate.

Until new-vehicle volumes are above 12 million units again, the returns from used-vehicle sales will be an important part of the financial picture for dealerships. In fact, returns to dealerships on a per-vehicle basis for used vehicles have increased by 39 percent in 2010.

So, where do we go from here? Obviously, it's vital for you to know where the auto industry is headed. A couple of weeks ago, I was all set to come here today and tell you how things were looking up in the auto industry! We're selling new cars again! Credit is available! Consumer optimism is on the rise!

Then the August sales numbers came out.

NADA's chief economist, Paul Taylor, isn't too troubled by the decline last month. For one thing, in August 2009, we were deep in the throes of Cash for Clunkers fever, so a year-over-year comparison is worthless.

And the industry has improved markedly since the lows of 2009, even though there is still work to be done on our overall economy. The auto sector – manufacturing and retail – have been two of the most robust parts of the economy.

As I am sure many of you have read, Wall Street and our housing industry continue to show weakness – not to mention 9.5 percent unemployment. The good news is that sales in 2010 are

on track to grow by double digits. Through the first seven months, sales were up fifteen percent. We expect that sales will be in the 11.2 to 11.7 million range for the year. But because consumers continue to be nervous, I'm concerned that a full rebound in retail demand is still not on the horizon.

The peak year for the industry was 2000, when we sold 17.4 million units. In 2001, even with September 11, the industry sold 17 million units. It was surprising that after that event we sold any cars at all. Compare those two years to what we saw between 2008 and 2010: Extremely depressed volumes, well below what was assumed to be a healthy industry of between 14 and 16 million units.

What is encouraging for our industry is that manufacturers, especially the Detroit Three – Ford, GM and Chrysler – undertook significant actions to lower their break-even points to allow for profitability at industry volumes below 11 million. Clearly for GM and Chrysler, the bankruptcy was the impetus for allowing their break-even to fall.

Looking at market share of the major players, it's no surprise that Ford has been a winner this year. Not having filed for bankruptcy has been of tremendous value to them as they attract customers to the Ford brand. With the introduction of the Ford Fiesta, it is likely that their momentum will continue.

We all know Toyota's challenges, and it shows – they have lost a full point of market share this year. Clearly, the recalls have had an impact on their once-untarnished image.

The big story of the past two years continues to be the success that the Hyundai Group has enjoyed. Hyundai and Kia have grown their market significantly – they have almost eight percent of the U.S. industry. Not so long ago, they were under five percent of the market.

The marketplace will remain competitive. Fiat is moving ahead with plans to build vehicles in Mexico for sale in the United States. Mahindra announced in August that they had been cleared to begin selling a small pick-up truck in the U.S. And at some point, the Chinese will arrive! New entrants in the market likely mean a very competitive new car marketplace and great opportunities for consumers.

Perhaps the biggest change we could see is new consumer purchasing behavior. As this economic crisis has unfolded, consumers seemed to be much more rational in their decision making. For the consumers who *are* purchasing, there seems to be a new "mindset." The days of bigger and more horsepower seem to have given way to smaller and more fuel efficient.

For example, the sport utility segment is in significant decline while the crossover utility segment is growing by 20 percent a year. The big benefits of crossovers are their car-like handling and better fuel efficiency.

For all the turmoil, there is evidence that the future for the U.S. market will be positive. It's encouraging that by 2015 we see the industry selling 17.4 million units. After all the misery of 2008 and 2009, it's refreshing to see a forecast above 15 million.

We learned some important lessons during this crisis, and they will help us as we move forward, especially in the uncharted territory of the new financial services world. One thing we found at the peak of the credit crisis is that the dealership model is not widely understood – by government officials, the media or the general public. I was amazed by how many times we had to educate people about how our business works.

For example, most people do not know that dealers own their inventory, that we purchase the cars and trucks from our manufacturers. The common belief is that manufacturers provide the inventory and we dealers just sell it. This misunderstanding can lead to bad public policy. I truly believe that government can be our partner and assist us, but it requires one-on-one interaction and a concerted and consistent effort to raise awareness among government officials about auto retailing and how it actually works in the marketplace.

Along with other NADA dealer leaders, I sat in multiple meetings with members of President Obama's administration and had lengthy discussions with his Auto Task Force, which was established to help engineer the changes needed at GM and Chrysler. This group was made up of Wall Street professionals with expertise in restructuring businesses. Members of the departments of Treasury, Commerce, Transportation and Energy also provided input. Our meetings with the Auto Task Force were essential to providing a greater understanding of what dealers do. And it allowed NADA to express concerns about the adverse effects of restructuring plans on dealerships.

As dealers, we need to continue to ensure that our lawmakers fully understand the vital role we play, not only in our country's national economy, but also in our local community. For example, dealerships helped to fund state and local government programs by collecting more than \$21 billion in sales tax revenue last year ... and that was in 2009, one of the worst year's in our history!

In addition to meeting with government officials, NADA spends a great deal of time maintaining an ongoing dialogue with all of the manufacturers. Having open communications proved invaluable as the crisis unfolded.

My point is, none of us can operate in a vacuum. By working together, we can move forward in the direction of profitability for all of us.

So when we began this battle over the financial reform bill, we had just spent over a year educating Congress, the Obama administration, the media, the public – anyone who would listen – on the vital role dealers play in our country's economy and in our communities, and we found that most of the people we talked to “got it.”

Congress certainly got it. They got that extending the bridge loans to the manufacturers was absolutely necessary. The failure of any of the Detroit automakers would have created not a ripple effect, but a tidal wave of unemployment and lost revenue to government on all levels.

They got that GM's and Chrysler's arbitrary termination of dealers was detrimental to our industry's and our country's economic recovery. And they got that dealer-assisted financing is good for consumers and for the continued recovery of the auto industry.

Now we – and I mean dealers and the financial services industry – need to educate regulators in the same way. We are committed to working with you to ensure that the new regulations are appropriate, effective and implemented as painlessly as possible.

It's the best way to keep credit available and affordable.

Thank you for inviting me to speak with you today. It's been my pleasure. Now I'd be happy to answer any of your questions. And please let me know if you have a question for Andy Koblenz, who is ready and *very* able to share his knowledge with you.

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