THE BIG SHORT (AGAIN)

Auto Loans Bubble Edition

ANOTHER HUGE BUBBLE ABOUT TO BURST

Parts 1, 2, and Remix

U/HAPPYEGG1000

The Big Short (Again) - Auto Loans Bubble Edition. Auto Loan Asset Backed Securities (ALABS): Another Huge Bubble About to Burst. - Dec. 28, 2021

Due Diligence

Check out Part 2 here after reading! (https://www.reddit.com/r/Superstonk/comments/rqpup4/the_big_short_again_the_auto_loan_asset_backed/)

Hey all! Welcome back to another DD but this time on a different type of Asset Backed Security. You probably know me now as the 'SLABS guy' (Student Loan Asset Backed Securities) due to my recent 5 Part DD Series on SLABS, but I figured at the request of many comments I'd take a deeper look at the auto market.

As many have pointed out, there are a ton of different collateral markets for different types of loans. Credit cards, medical, auto, student loans, etc. I am of the belief that these ABS markets are all inherently risky, as the regulatory measures like ratings have been corrupted in the pursuit of money. I decided previously to look into the Student Loan ABS bubble because of how big the market was - about $1.6T in student debt is held by the USA total. I didn't even realize that the auto market has about the similar amount of debt outstanding - approximately $1.3T. Wow. Time to go down this rabbit hole for a bit. SLABbit hole? ALABbit hole?

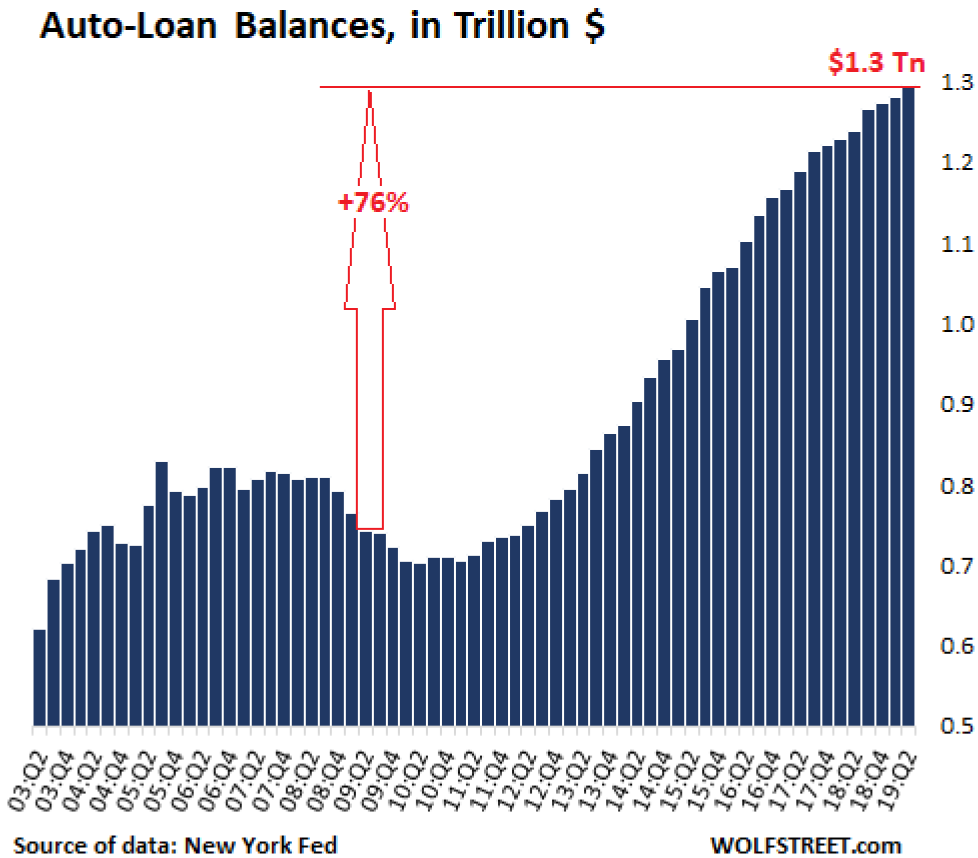
This is the first time I've ever really looked into auto loans and the securities market associated with them. So take this with a grain of salt. We're all still learning here.

With that said, let's go! This is gonna be a fat DD. I'll include a TL:DR at the bottom, but I'd still recommend reading the whole thing.

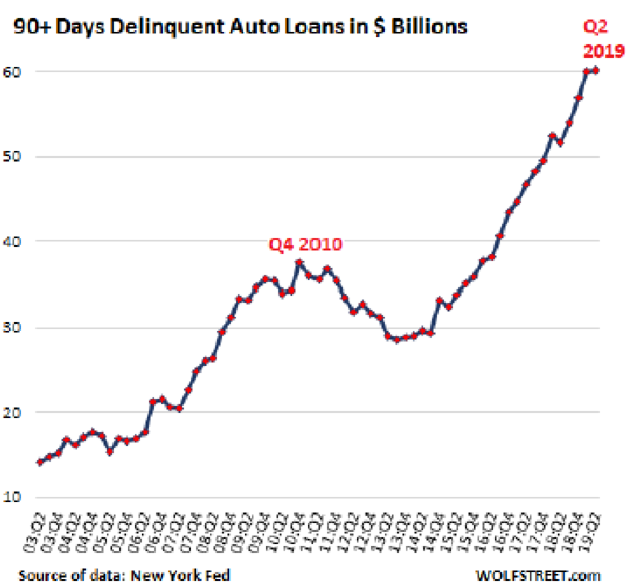
First of all, the structure of Auto Loan Asset Backed Securities (ALABS) functions very similarly to how SLABS work, or Mortgage Backed Securities worked back in 2008. This link (https://www.stockmarketloss.com/securities-law/auto-loan-backed-securities/) explains: *"Subprime auto loans have been and are being bundled into auto loan asset-backed securities (“ABS”) and sold to the public as solid, income-producing debt investments similar to corporate bonds. They’re marketed as secure products offering above-average interest. But while a bond may be backed by an issuing company’s income and assets, these auto loan ABS products are backed solely by a pool of auto loans. The loans are bundled and the rights to receive the payments generated by the loans are sold to investors. Those rights are divided into tranches."* Tranches? Subprime loans? Asset backed securities that are misleadingly marketed as secure products? That all sounds familiar.

But first, let's discuss how big the market is for these ALABS. I will be extensively referencing this study for information, and using graphs with data from the New York Fed. The study is entitled "Bursting The Auto Loan Bubble In the Wake of Covid-19". Well that title is straightforward isn't it.

It's important to understand just how many people take out loans to buy cars. *"About 85% of Americans own a car, and 2/3 of car owners fund their ownership with loans".* So obviously, even though these loans will not have larger dollar values than student loans or housing loans, they're still very widely used. And they're growing. A lot. This graph should help demonstrate this rise further. It uses data from the New York Fed.



The study continues, saying *"During the past decade, auto debt has skyrocketed, increasing nearly 40 percent overall, with the average auto loan for a new car rising 11 percent. Part of the growth stemmed from a flourishing subprime auto loan market, which now accounts for nearly one-quarter of the $1.33 trillion in auto loan debt outstanding. Overall, as of the beginning of 2020, auto loans made up about nine percent of household debt, making "[t]he auto loan market . . . the third-largest consumer credit market in the United States," behind home loans and student loans."* Ummmmm...this should be a HUGE red flag. The subprime (aka ' very risky loans that probably never should've been given out') market alone makes up nearly $325B (a quarter of $1.33T) of the auto loan industry! And with this growing amount of subprime loans comes increasing levels of default. Just look at this graph here, compiled also from data from the New York Fed.



You can see a DRASTIC rise in auto loan defaults which as I believe is a result of increasing lending to subprime consumers. So why hasn't the bubble burst yet? Well, that same study says *"Prior to the pandemic, the build-up of auto loan debt outstanding and the growth in delinquencies and defaults led experts to classify the auto loan market as a bubble and to predict that the bubble would burst soon. The United States' strong pre-pandemic economy combined with a low unemployment rate likely were the leading reasons that the bubble did not burst at that time. Yet, even then, multiple reports recognized that the rise in auto debt in the United States showed an unsustainable dependence on automobiles financed by households."* Ok. So the reason that shit hasn't hit the fan yet is because the economy was really strong before the pandemic. Well, here we are a few years into the pandemic now, and this thing still has not burst yet. In my eyes, it's only a matter of time.

A reason why defaults and delinquencies may be increasing is because people are strapped for cash recently, with inflation and now the pandemic. This article (https://www.stockmarketloss.com/securities-law/auto-loan-backed-securities/) states, *"Borrowers with more cash than credit tend to pay their loans more quickly to avoid the high interest rate attached to the loans. The fact that they're paying loans more slowly is thought to be a sign that borrowers are more strapped than they have been previously."* Basically, people are paying loans more slowly, which causes interest to snowball, and will thus cause even more risk of default.

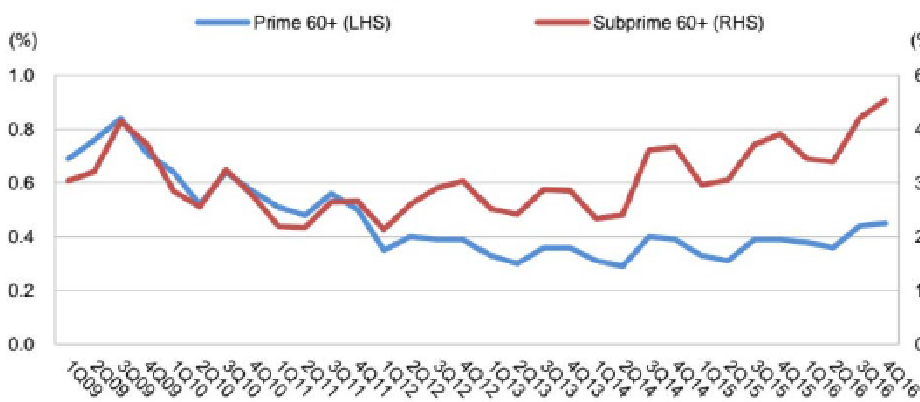
Another interesting thing to note is how auto loans actually work. While some large companies have in-house crediting, like Ford Motor Credit, typically banks partner with dealerships who then give loans to customers. This is a huge issue. Because **instead of these banks directly servicing consumers, they are instead trying to please dealerships the most.** This means that *"the auto loan origination market prioritizes the interests of lenders over those of customers, which has led and will continue to lead people to agree to loans with disadvantageous (and inflated) interest rates, fees, and terms."* Pretty straightforward - because the dealership is the middle man who is actually giving the banks business and money, the banks negotiate loan terms that are *more favorable* for the dealers than the buyers. This would obviously lead to increased rates of delinquency and default, but this strategy is still *immensely profitable* for dealers. Take a look. *"Over the past decade, the relative proportion of profit that auto dealers have made from car sales versus car financing has narrowed. For instance, in 2011, dealers made 66 percent of their profit from car sales versus 34 percent from car financing. In 2018, this balance had flipped, with dealers making money from car loans than car sales. Dealers should be increasingly more interested in selling auto loans than actual cars."* Woah. So now, **when you go to buy a car, the dealers are actually more interested in putting you into debt and making money off your loan than making a profit off the physical car.** That's pretty wild to think about.

How is this even allowed? Well, the study continues, saying "*Similarly, as noted by Edward Balleisen and Melissa Jacoby, car dealers have succeeded in lobbying at the state level, leading to the lack of state-level regulation of auto loans, and have a lobbying force that is ready to take on proposed regulations."* Try to act surprised.

But how does all of this tie into an ABS market? Well, similarly to other types of loans, *"Auto asset-backed securities are essentially a bundling of car loans that are then sold to investors. They are grouped by the creditworthiness of the borrowers and categorized as prime, nonprime or subprime."* (Link). As I explained in my DD about SLABS, the record-high levels of RRP show that everyone is absolutely desperate for collateral. So I would not be surprised if these ALABS were also being used extensively as collateral. But, as I've shown above, these ALABS are again overvalued. That article continues, saying *"Delinquency rates are on the rise in auto ABS, especially in the subprime category. According to a May 2018 story in PYMNTS, "subprime delinquency for loans more than 60 days past due reached its highest since 1996 at 5.8 percent." That number, according to Business Insider, was a jump of 0.6 percent from the year prior and up 2* *percent from the same time period in 2014. Perhaps even more telling, according to PYMNTS, the default rate leading up to the 2008 financial crisis was around 5 percent."* Well shit. We already know that subprime loans make up a pretty damn big percentage of all auto loans. And if defaults are on the rise, then obviously the ALABS market is being strained. This article also says that *" Bloomberg reported in April that two smaller subprime lenders – Summit Financial and Spring Tree Lending — filed for bankruptcy while Pelican Auto Finance shut down completely. Furthermore, the publication notes that rising interest rates will likely make things more challenging for these lenders."* This again is a pretty big red flag. These subprime lenders going under signals a *significant* risk that these subprime loans are dogshit, and their value is finally coming down to Earth.

Even Morgan Stanley is calling out this bullshit. As Walter White once said, *'you can't bullshit a bullshitter'.* This link reads, *"Morgan Stanley has stated: "In fact, since 2010, the share of Subprime Auto ABS [asset-backed securities] origination that has come from these deep subprime deals has increased from 5.1% to 32.5%.[2]" Subprime loans are those made to people with low credit scores. While there is no standard definition for "subprime," it often refers to people with credit scores lower than 640, and "deep subprime" refers to credit scores lower than 500. The lower the borrower's credit score, the more likely the borrower is to default on a loan. Accordingly, subprime loans are inherently riskier than prime loans and deep subprime loans are riskier still."* Again, this highlights how the bottom line of this market is about to go down the shitter. This graph demonstrates even further.

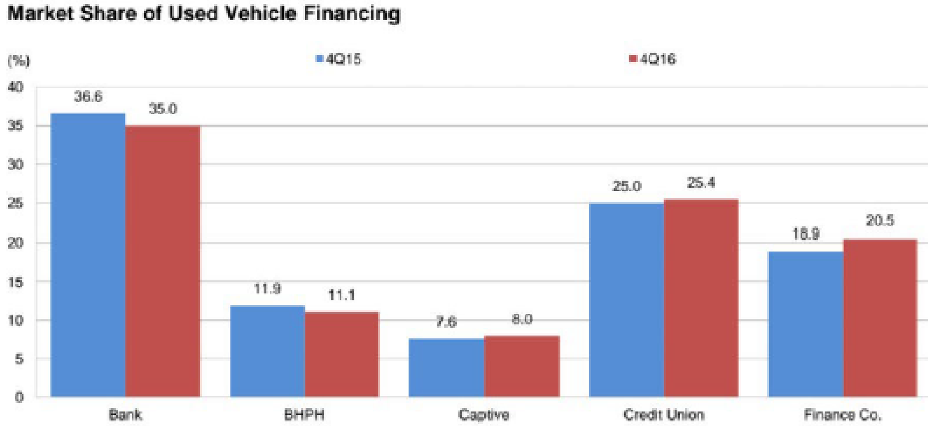
Fitch Auto ABS Indices: 60+ Day Delinquencies



Note: Data reflect the last month in each quarter.
Source: Fitch.

It's similar to the graph I showed previously. But this one highlights how these prime and subprime markets have drastically diverged recently. And like I mentioned, banks are starting to notice. As far back as 2016, banks started decreasing their exposure to ALABS, while independent companies have taken up this slack. Hence why like I previously mentioned, it was these smaller players beginning to go under.

Market Share of Used Vehicle Financing



Source: Experian-Oliver Wyman Market Intelligence Reports.

As you can see, banks decreased their exposure by 1.6%, with private finance companies increasing their exposure by 1.6%. These graphs are from this source.

But there is YET ANOTHER problem. As I'm sure you're aware, cars are essential to American life. And **this has led some people to get desperate enough to get a car to commit fraud.** This source states that *"Given the higher risk inherent in subprime loans, one would hope that borrowers are being forthright in their loan applications and that lenders are being thorough in their due diligence. Unfortunately, it appears that neither may be happening. Bloomberg reports that "as many as one in five auto-loan borrowers admitted in a survey that their applications for debt contained inaccuracies . . . meaning fraud could be more pervasive than lenders planned for."* Oh great. So not only do we have to deal with the risks of companies giving out subprime loans to people with horribly low credit scores, but we also have to deal with people lying about their financial situations to get a loan at all, which would expose this industry to even more risk.

But it's not just borrowers who aren't doing their due diligence. This same source continues, saying *"Unfortunately, as borrowers' inaccuracies or falsehoods increase, lenders are growing lax in their data verification. It was reported recently that Santander Consumer USA Holdings, Inc. – one of the largest subprime auto finance companies – verified income on a mere 8% of the borrowers whose loans it bundled into $1 billion of bonds. Santander agreed to pay nearly $26 million in settlements with Massachusetts and Delaware related to allegations that it facilitated unfair, high-rate auto loans for thousands of buyers. Naturally those loans were packaged into securities sold to investors. Santander is, however, not alone in its income verification procedures. Americredit, another large auto-loan company (and a unit of General Motors Financial Company), reportedly verifies only 64% of its prospective borrowers' incomes."* **So not only do you have one in five auto loan borrowers committing fraud to get a loan. You also have lenders who are straight up not checking the credit scores and incomes of people they're giving loans to.** And why would they? Again, like I mentioned earlier, the profit for dealerships now comes from making people take out as many loans as possible. Holy shit. Hello, 2008 again.

Here's the bottom line. Via this source. *"If the underlying loan slow payments and defaults are significant enough, it is possible that investors won't receive the interest they expected to receive. The bond values will then decrease on the open market. Investors trying to unload the under-performing or non-performing bonds may only be able to sell them at a loss, if they're able to sell them at all. If the underlying loan performance is bad enough, some of the bonds themselves could go into default, meaning that the principal sums due are never repaid. Investors face the possibility of losing some or all of the money invested in these supposedly safe bond or bond-like investments. The bottom line is that auto loan ABS investments are not safe, secure, and better paying bonds or bond alternatives. They are subject to major losses and will become increasingly risky as car loan defaults continue to increase."* This quote really just speaks for itself. This is a bubble, and a big one.

So who's left holding the bag if this goes to shit? Here's what this source thinks. *"The most aggressive have been specialized lenders, including small shops backed by private equity firms, and larger lenders such as Santander Consumer USA. But they're spreading the risks to investors by packaging their loans into subprime auto-loan backed securities, of which the highest-rated tranches have AA or even AAA ratings. And these securities are everywhere, from bond funds in the US to some pension fund in a Scandinavian city. For investors and lenders, these delinquent loans don't represent total losses. If the default cannot be cured and the lender decides to repossess the collateral – which is easy to do with modern tracking technologies – the lender obtains a used vehicle for which there is a liquid auction market (unlike housing) with wholesale auctions around the country, and finding a buyer is generally not the problem. The problem is the difference between the price at auction and the outstanding loan amount. The difference plus expenses is the loss that the lender and investors take. This loss might be 50% of loan value."* Yup. So it looks like a whoooole lot of people are about to be exposed to significant losses in their portfolios. Wonderful.

Now, it's time for a TL:DR.

TLDR: Auto Loan Asset Backed Securities are similar to Mortgage Backed Securities and Student Loan Asset Backed Securities. When loans are taken out to buy a car, these loans are then packaged into ALABS, which are then sold to investors who reap the interest rates. However, these ALABS are posing increasing risk of devaluation, due to increased numbers of default rates due to the pandemic, the drastic increase in the usage of subprime (shitty) or deep-subprime (most shitty) loans, fraudulent reporting by borrowers, incomplete due diligence on part of lenders, and slow loan payments. This relates to GME, as if these ALABS lose value, they also lose value as collateral. RRP has shown how desperate people are for collateral, so the thesis is that ALABS are being used extensively as collateral. Devalued collateral = banks get scared and raise margin requirements = margin calls = MOON. Not to mention that even if these aren't being used as collateral, tons of investors are exposed to these things, so a recession would ensue which I believe would also cause margin calls.

Thanks so much for reading you guys! We'll see if there will be any further parts. Originally I planned for my SLABS DD to be one part, yet I'm already on Part 5. As always, I will write more parts if more new information comes to light via comments or DMs. So please, put me onto some more leads!

One final thing. I am not a financial advisor. Please do not ask me how to make money off this situation. My personal investment strategy has been all GME, and this information does not change that. as always, I believe GME to be the best hedge against a market crash. Thanks again, and make sure to check out Part 2.

The Big Short (Again) - The Auto Loan Asset Backed Securities (ALABS) Bubble Part 2: Ratings Agencies, Used Car Prices, Santander Drive Auto Receivables Trust (SDARTs), Trade-In Treadmills, Bombshell Reports/Lawsuits, and more. This is BAD. - Dec. 28, 2021

Due Diligence

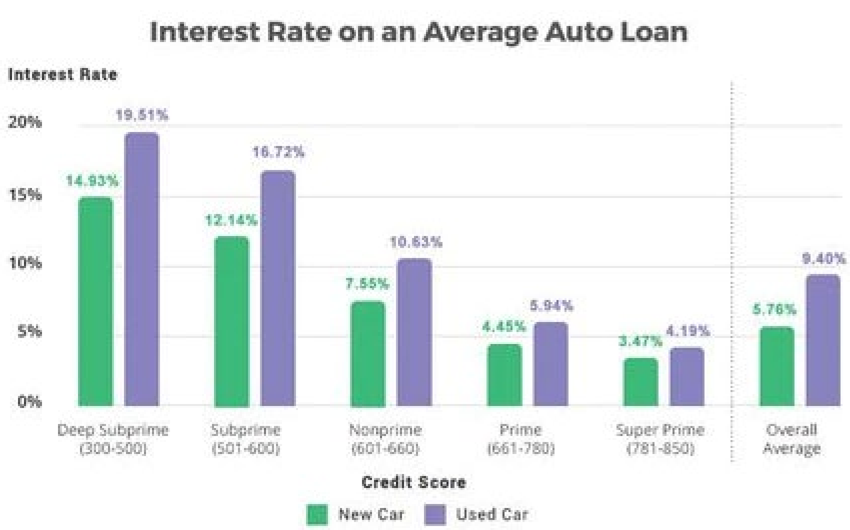
Oh boy. Realizing now that my first DD barely scratched the surface of these ALABS. I foresee writing in my future. Thank you all for your concern for my health and wellbeing! I love writing and researching this stuff. If I need a break, I will absolutely take it. But for now, I'm too interested in all this to just walk away.

You can read my Part 1 here. Obviously I'd recommend that before jumping into this one. Also make sure to check out my SLABS DDs. So many bubbles, so little time!

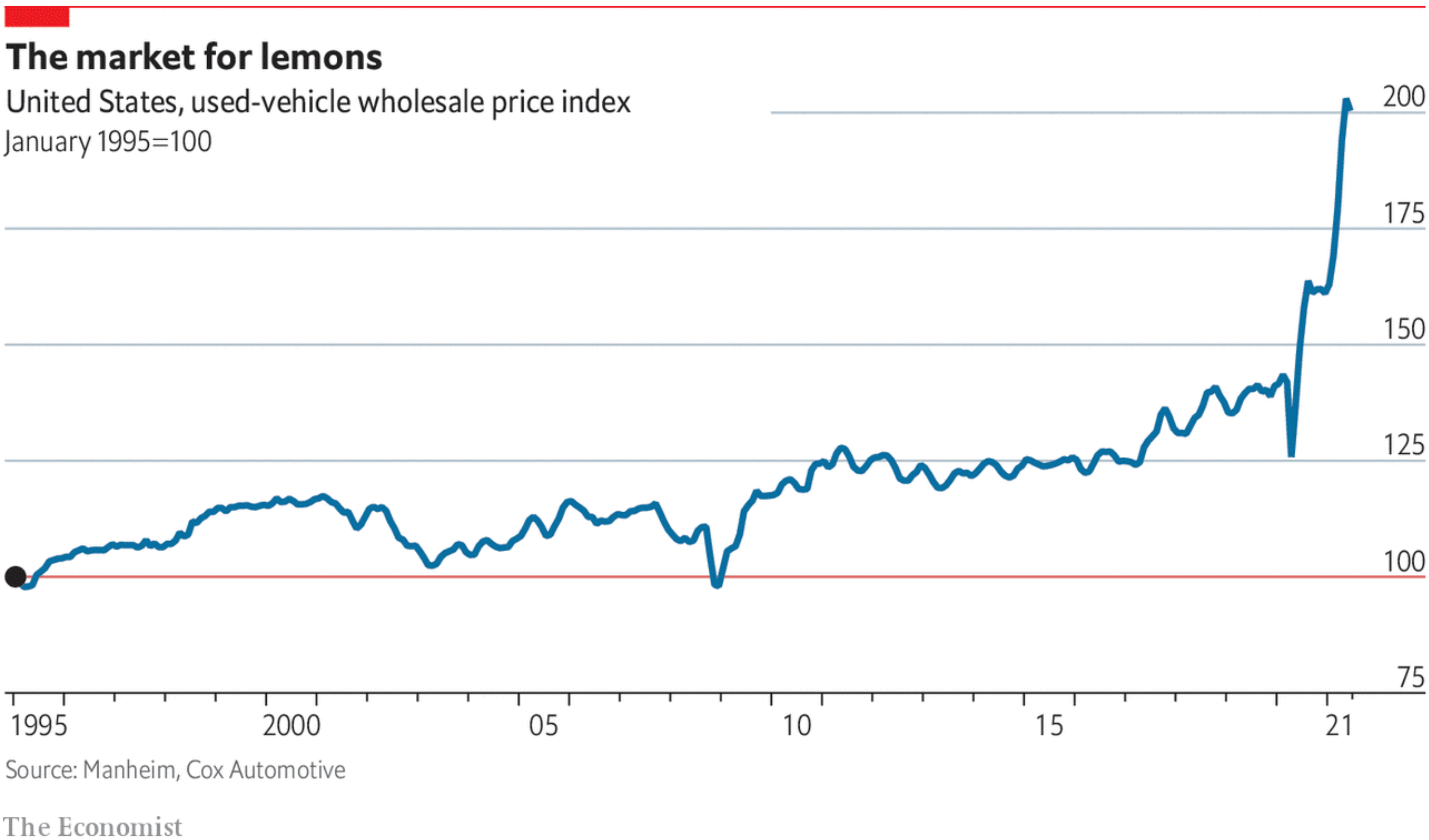
I don't really have any corrections I'd like to make to my first part. If that changes, I will edit this post, or include the edits in a Part 3, if it happens. Let's go!

First of all, I'd just like to quickly mention that the way these loans are rated works the same as most other asset backed securities. Yup, the same exact conflict of interest exists here as it did in 2008. Ratings agencies like Moody's and S&P are paid by the servicers of ALABS to rate these very ALABS. Just thought I'd bring that up here, as it helps to link all different types of ABS - the same scumbag rating agencies are involved with many different types.

Next up, used car prices. I didn't really address appropriately in Part 1 why I believe the used car market is so hot, and the significance. So here goes. The used car market being hot greatly benefits ALABS. The more loans have to be taken out, the more money these dealerships make from these loans. Obviously, the main cause of the hot market the insane chip shortage. There just is not enough supply of new cars to satisfy demand. u/Vnmous, who works in the auto industry, had a great comment on my first part, saying "*Dealers are enjoying the position of the industry at the moment. They have never made more money, even though there are no cars on most lots".* My part 1 DD supports this conclusion: dealerships now make a majority of their profit on loans, not profits from the physical car. Here's a graph that shows why this hot used market benefits these dealerships.



Interest rates are *significantly higher* for used cars. This means that dealerships are making more money off used car loans. Interesting. This has led them to dealerships buying back used cars that they previously sold and selling them again - many dealerships are offering high compensation for used cars you bought from them previously. However, this comes with a problem. Because the majority of cars available now are used, people are taking out more and more expensive loans due to the increasing interest rates AND the meteoric rise of used car prices, as shown by this graph.



This, in my opinion, has caused a significant increase in the probability of defaults and delinquencies, which will affect the bottom line of these ALABS.

Now, let's talk about Santander Drive Auto Receivables Trust, or SDARTS. These are a little complicated, so get ready for some reading. Per [this source](), *"One of the more popular auto loan-backed securities is the Santander Drive Auto Receivables Trust ("SDART") product. The SDARTs offered bonds categorized into different classes – a number of A class bonds, followed by B, C, D, and E class bonds. The payoff time was to be longer for each successively higher class, leading to greater risk but higher interest rates for the lower classes. An analysis of the SDART offerings shows the cumulative effect of rising defaults and slower payoffs in underlying loans.*

Beginning with the first SDART issued in 2013, the payouts started growing longer. Whereas the October 2012 offering had the Class B payout to be completed in May 2017, the January 2013 offering called for the Class B payout by January 2019. Stated differently, a product offered four months later pushed the payout seven months out. While all of the SDART products offered through the end of 2012 are fully paid and retired, all of the products offered thereafter have one or more classes of debt still outstanding.

It seems that the trend of slower borrower loan payments is having the direct effect of causing these products to run for progressively longer periods of time. While that means that those who own the various bond classes enjoy the interest *return for a longer period of time, it also means that they're subjected to the risk inherent in the product for a longer period as well. As auto loan default rates climb, it is possible that the ratings agencies will downgrade the riskier debt classes, making it more difficult to sell those instruments on the open market."* Ok. Allow me to do my best to summarize. SDARTs are a type of auto-loan backed ABS. There are different tiers, ranging from A to E, with the risk exposure and interest rate increasing with each tier. However, due to borrowers having less money in general due to inflation and the pandemic, loans are taking longer to repay. **This is exposing what was supposed to be the low risk tiers, (like A and B) to as much risk are the lower tiers were previously exposed to. And now, the lower tiers are *even riskier.*** Basically, these SDARTs just got a whoooole lot riskier. And they're extremely popular.

Now, I'd like to talk about Trade-In Treadmills. This quote, via this source, should explain things a little better than I could. *"In a note out March 27, Moody's highlighted what it called a "trade-in treadmill." In other words, auto lenders are choosing to roll negative equity at trade-in in to the next vehicle loan.*

It looks a little like this:

1. *Car Buyer acquires a Truck 1 for $100, taking out a $80 loan to make the purchase.*
2. *Truck 1 drops in value by half by the time Car Buyer decides to trade in.*
3. *In that time, Car Buyer has only paid $10 of the loan, leaving him/her with $20 in negative equity ($80 loan minus $10 payment minus $50 trade-in)*
4. *Car Buyer rolls the $20 negative equity in to the next loan on the next purchase.*

From Moody's note: The percentage of trade-ins with negative equity is at an all-time high, as is the average dollar amount of that negative equity. Lenders are increasingly faced with the choice of taking on greater risk by rolling negative equity at trade-in into the next vehicle loan. We believe they are increasingly taking this choice, resulting in mounting negative equity with successive new-car purchases. This "trade-in treadmill" generates higher loan to value ratios, slower principal amortization and higher loss severity when defaults occur." Woah. This is a pretty big issue. **You have these loans that are just going to keep snowballing on each other because people are paying loans slowly, trading in their cars, and rolling over their negative equity.** Yikes. And we know that the ratings agencies are just as corrupt as 08. So I would not be surprised if these are still being rated AA or AAA.

Now, I'd like to talk about an absolute bombshell of a report done by ConsumerReports into the true state of the auto loan industry. This was absolutely mindboggling. This article summarizes the report, while the actual ConsumerReports article can be found here. Here's a quote from the summary: "

The investigation found:

- ***A credit score doesn't necessarily dictate the terms of the loan offered.*** *Borrowers in every credit score category—ranging from super-prime, with scores of 720 and above, to deep subprime, with scores below 580—were given loans with APRs that ranged from 0 percent to more than 25 percent.*
- ***Some high credit scorers get high-priced loans.*** *While, on average, borrowers with low credit scores are offered the worst terms, about 21,000 borrowers with prime and super-prime credit scores, about 3 percent of the total borrowers in that group, received loans with APRs of 10 percent or greater—more than double the average rate for high scorers in our data.*
- ***Many borrowers are put into loans they might not be able to afford.*** *Experts say that consumers should spend no more than 10 percent of their income on an auto loan. But almost 25 percent of the loans in the data CR reviewed exceeded that threshold. Among subprime borrowers, that number is almost 50 percent, about 2.5 times more than prime and super-prime borrowers.*

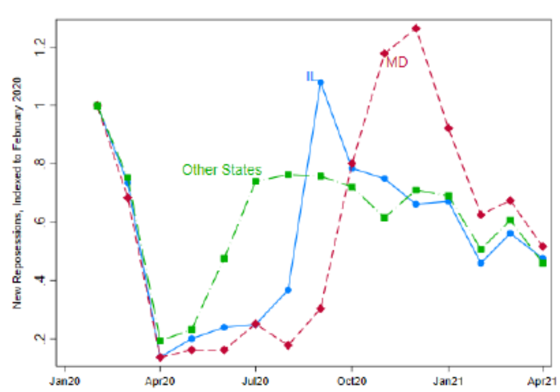
Underwriting standards are often lax. *Lenders rarely verified income and employment of borrowers to confirm they had sufficient income to repay their loan. Of the loans CR looked at, these verifications happened just 4 percent of the time.*

- ***Delinquencies are common.*** *More than 5 percent of the loans in the data — 1 in 20, or about 43,000 overall — were reported to be in arrears. While delinquencies declined over the past year and a half, likely thanks to pandemic-related deferment programs, industry groups and regulators are bracing for a potentially sharp uptick in the coming months."* **Holy SHIT.** This is worse than I thought. You have even prime and superprime buyers being subjected to horribly high priced loans, borrowers being put into loans that these companies know they can't afford, companies not checking incomes to even verify the likelihood of repayment, and a ton of delinquencies. I don't even really know what to say at this point. The value of these ALABS are honestly jack shit. But the bubble hasn't burst yet.

Now, I'd like to talk about some pretty high profile lawsuits that show just how scummy these auto loan agencies are. First up, some quotes from this source. *"Early last week, Attorney General Maura Healey filed a lawsuit against Credit Acceptance Corporation ("CAC"), a credit lender that specializes in auto loans. The complaint alleged that CAC had provided borrowers with high-interest subprime auto loans which the company knew the borrowers would be unable to repay. After borrowers defaulted, CAC aggressively pursued them for repayment, hailing them with collections calls and overcharging them for their deficiencies. The company then misled investors by packaging these high-risk loans along with other loans into asset-backed securities, which CAC misrepresented as only containing high-quality loans. As a consequence of CAC's activities, thousands of consumers have been left in financial ruin. Borrowers of these loans risk lowering their credit score, losing their automobile, and facing accumulating fees if they default.*

CAC is not the only company in the subprime auto market to be recently accused of deceitful and predatory behavior. Earlier this year, Santander agreed to a $550 million settlement with 33 states and the District of Columbia after engaging in similar conduct, approving high-cost auto loans for consumers with subprime credit. Last year, Exeter Finance paid $6 million as part of settlements with Massachusetts and Delaware based on their subprime auto loan practices as well. These lawsuits illustrate a growing and concerning trend in the auto finance industry– more and more credit lenders have been willing to offer loans without engaging in reasonable underwriting practices." This basically confirms all of what I previously described with that ConsumerReports article (also, Santander? Sound familiar? Hint hint: SDARTs). Companies are giving borrowers loans they can't repay, just to make more money off these loans. **It's really an infinite money glitch - first they get the money from the insanely expensive loan they gave you, then they just go and repo your car anyways. In some ways, ALABS are even worse than SLABS in the aspect that because there is very valuable physical collateral in the form of a used car, companies have incentive to drive consumers into default so they can repo the car and resell it.**

Just look at what happened to repossessions once repo moratoriums ended. Illinois and Maryland ended their pandemic repo moratoriums separately from other states, so you can really see how big an impact this had. (Via this article).



Looks like repos are through the roof, likely due to all the previous factors I mentioned.

Now, it's time for a TLDR.

TLDR: The used car market is very hot right now due to supply shortages. This greatly benefits dealerships and therefore increases the creation of ALABS. However, these ALABS are really bad quality because of how expensive used cars are and how much higher interest rates are. Additionally, companies have been giving out loans so expensive there is little chance of repayment, even for prime and superprime borrowers. While these companies have been challenged by lawsuits, the system has yet to see major changes, and the fines were likely a slap on the wrist compared to how much profit these guys are making. **Companies really have a sort of infinite money glitch - give out exorbitant loans, collect money on those loans, the borrower is still forced to default due to the near-impossible-to-repay fees, dealerships repo the car, and they run the same scheme on another sucker.**

That's about all I've got for this part. Again, I'll make more parts in the future if I come across more new info. Thanks again for reading.

One final thing. I am not a financial advisor. Please do not ask me how to make money off this situation. My personal investment strategy has been all GME, and this information does not change that. as always, I believe GME to be the best hedge against a market crash. Thanks again.

The Big Short: Remixed. A Summary of My DDs on Auto Loan Asset Backed Securities. This is pretty huge.

Due Diligence

Hey all. If this title seems familiar, you may have seen a similar post several days ago about my research with Student Loan Asset Backed Securities, or SLABS. That post got a ton of attention and helped expose my SLABS DD's to a wider audience. The goal of this post is similar, but to increase exposure to my DDs on Auto Loan Asset Backed Securities, or ALABS. This bubble is as if, if not more important than SLABS, but the ALABS DDs haven't reached the same level of exposure on the sub. There is about as much outstanding student loan debt as there is auto loan debt, with approximately $1.6T and $1.3T respectively, so I feel these bubbles should receive similar attention. Also, since both ALABS parts are decently long, I figured a summative TL:DR would aid with understanding.

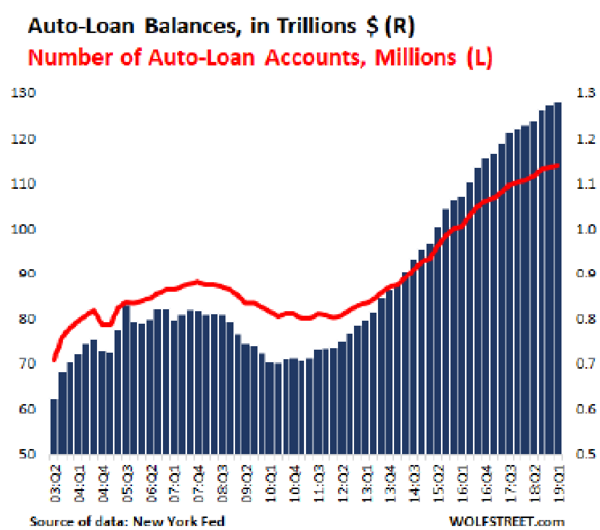
You can read Part 1 of my ALABS DDs [here](), and Part 2 [here]().

The thesis: ALABS are a very similar to the subprime mortgage backed security market that caused the 2008 recession. Basically, ALABS are tranches of auto loans packaged into a security and sold to investors. Investors can reap the benefits of interest rates on these ALABS. Pretty similar to SLABS, just with auto loans. *The same rating agency issues in 2008 and with SLABS that I pointed out are still present here, even including many of the same companies like Moody's and S&P.* It's just bubbles on top of bubbles with these guys. In fact, I believe this bubble to be even larger than SLABS because you don't have to deal with federal vs. private loans, pre-2010 or post-2010 distinctions, etc.

ALABS have increased along with the not-coincidental recent meteoric increases in both used and new car prices. We know that everyone is desperate for collateral right now, as shown by the record breaking RRP. This gives me reason to believe that ALABS are being used extensively as collateral. ALABS, like SLABS, are *drastically overvalued*, and are about to come crashing back down to Earth as a result of several factors. However, possibly unlike SLABS, investors will be MAJOR bagholders in the event of a crash, and bagholders are much more widely distributed. So even if these aren't being used as collateral (which is highly, highly unlikely), the ensuing recession after these things shit the bed would still have the same effect, which is margin calls. This is how I believe it ties into GME. Plus, it's just interesting to learn about how fucked our system is. Anyways, here are those factors. Sources can be found in my DDs. This is just a TLDR.

-First of all, ALABS are nearly as extensive as student loans. About 85% of Americans own a car, and 66% of car purchases are completed with the help of a loan. This graph should really drive home how much we Americans are taking out auto loans.

https://wolfstreet.com/wp-content/uploads/2019/05/US-auto-loan-balance-v-number-2019-01.png



-Of these loans, a large percent (about 25%) are subprime or deep subprime, aka shitty and shittiest. This is a very large amount of exposure to high risk loans. And it's only increasing. However, the same ratings conflicts of interests exists, as ALABS servicers pay ratings agencies to rate their ALABS, so a large percentage of ALABS are still being rated AA and AAA. Fuck.

-Borrowers are paying back their loans much slower due to money troubles with inflation and the pandemic. And since now used cars are what most people are buying, and used cars have insanely high interest rates, the amount to be paid back just keeps snowballing and snowballing.

-Loaning companies allow you to roll over any negative equity from previous loans, increasing payments further. Also, loan companies rarely actually check borrowers' income (and why would they? they want your loan money), about 1 in 5 borrowers actually commits fraud and lies about income to be able to buy a car, and loan companies are issuing EXORBITANT loans (so much so that even prime and superprime loaners are having difficulty paying).

-Banks, instead of servicing borrowing directly like they do SLABS, make deals with dealerships, who then provide the loans to buyers. So, the *banks' real customers are dealerships*, who they aim to please first and foremost. This leads to elevated interest rates and fees which benefit the dealerships, but very unfavorable conditions for the borrower.

-Many smaller subprime auto loan companies are going under. This is a huge warning sign, because these companies have been increasing their exposure, while banks have been decreasing their exposure. So it's actually more important to pay attention to the little guys.

-The holders of these ALABS are extensive. They are in pensions, held by normal investors, in ETFs, etc. Lots of exposure, possibly moreso than SLABS.

-TLDR for the TLDR: Rolling over negative equity, insanely expensive predatory loans, extensive loaning to subprime and deep subprime customers, lack of due diligence from loaners, fraud from desperate buyers, and dealerships being the middle man for loans instead of a direct bank-consumer link all mean these ALABS are losing value FAST. They're dogshit wrapped in catshit. Defaults are also increasing a fuck ton. And what happens in a default? Yup, they repo your car.

It's an infinite money glitch - issue impossible loans, receive loan payment, borrower still has to default, repo the car, and start all over again with someone else.

Thanks for reading this summary. I hope it encourages you to look further at my DDs.

One final thing. I am not a financial advisor. Please do not ask me how to make money off this situation. My personal investment strategy has been all GME, and this information does not change that. As always, I believe GME to be the best hedge against a market crash. Thanks again.