



**2016 USED CAR MARKET REPORT**

21ST EDITION



# 2016 USED CAR MARKET REPORT

## 2 A NOTE FROM JANET BARNARD, PRESIDENT, MANHEIM NORTH AMERICA

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## 4 YEAR IN REVIEW AND OUTLOOK

Autos have been a gem in an otherwise dull economy, with new unit sales in 2015 up 68 percent from 2009's trough. Auto loans outstanding have grown from \$700 billion in 2011 to over \$1.1 trillion today.

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## 12 REMARKETING INDUSTRY OVERVIEW

NAAA-member auction sales rose 6.3 percent in 2015 to 9.3 million units, and volumes will continue to rise in 2016 and 2017. Meanwhile, wholesale prices have been on an elevated progression for six years; increases in 2015 brought prices to near-record levels (just 1.2 percent short of the 2011 high). With wholesale auto transactions taking place through numerous buying channels, technology tools emphasizing speed and efficiency are more critical than ever.

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## 22 DEALERS

New vehicle sales increased for an unprecedented sixth consecutive year, and the total, 17.5 million, was a record. Franchised dealers also recorded increased used vehicle sales for the sixth straight year, while a record 2.5 million certified pre-owned units were sold. Dealers consigned 56.5 percent of all units sold at wholesale auctions in 2015.

- // Q&A with NADA Chairman Jeff Carlson
  - // Q&A with NIADA President Frank Fuzy
  - // Q&A with Raj Sundaram, Cox Automotive
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## 45 RENTAL

Total rental car industry revenue reached a record \$27.1 billion in 2015 even though revenue per unit remained flat. A downward adjustment in fleet size should allow for better revenue-per-vehicle numbers in 2016.

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## 54 LEASING

New lease originations reached an all-time high in 2015, just shy of 4 million units. An increase in off-lease returns in the years ahead will lead to an increase in CPO sales. In 2015, for example, CPO sales and off-lease volumes were nearly identical.

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## 62 REPOSSESSIONS

The auto finance market topped \$1 trillion in loans outstanding in 2015 thanks to record new vehicle sales and higher used unit volumes and pricing. Despite exceptional portfolio performance, repossessions grew modestly simply because of the larger number of contracts outstanding.

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## 70 FLEETS

New vehicles purchased by commercial fleets grew by more than 2 percent in 2015 to 629,000 units, the sixth consecutive yearly increase. While government fleet purchases declined slightly, commercial fleet purchases should continue to grow as a result of higher employment levels.

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## 78 SALVAGE

In 2015, the salvage marketplace experienced an increase in volume and moderate decrease in prices, while overall demand remained strong. Total loss vehicle prices dropped in concert with a decline in scrap metal prices. Consignors continue to sell an increasing number of clean-titled vehicles in salvage lanes when the vehicles have excessive miles or wear and tear.

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## 82 INTERNATIONAL

Passenger car sales reached a record 89.4 million worldwide in 2015, with China retaining its position as the largest car market even though sales stagnated there. With U.S. new car sales continuing to rise and demand for vehicles strengthening in developing countries, look for a significant spike in used car exports.

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## 92 COX AUTOMOTIVE

**2016 USED CAR MARKET REPORT**

# **A NOTE FROM JANET BARNARD**



## WE LIVE IN AN AGE OF ENDLESS POSSIBILITIES.

And, this reality is accelerating, as previously unforeseen developments seem to arise every week. It requires us to think more deliberately about our direction and how we will invest resources, focus our time and meet changing client needs. We've reached a point in our industry where our efforts depend upon strategic vision and intent.

For Manheim, this means delivering innovation, empowering our dealer and commercial clients with new products and services, and leading positive change in our industry.

As we look ahead to 2016 and beyond, Manheim will strive to create greater levels of efficiency, enhance the client experience, and partner with clients for success.

To support these objectives, we encourage you to explore the many facts, figures, and trend analyses highlighted throughout our 21st annual edition of Manheim's Used Car Market Report.

### **Drive Greater Levels of Efficiency**

We recognize that efficiency is the new currency for our business. It is critical, especially in light of client demands for speed and delivery, to support their profitability and future growth. They seek greater levels of productivity in every aspect of their—and our—operations. In response, Manheim's services range from helping clients buy and sell vehicles efficiently via physical and digital channels, to improving the wholesale-to-retail process by reducing time and steps associated with reconditioning, inspections and delivery.

### **Enhance the Client Experience**

We believe delivering the optimal client experience will be the differentiator. That's why we are investing more than \$150 million to develop new mobile apps, online self-service tools, financial solutions, and more to enhance the experience for our clients and provide remote access to live sales anytime, anywhere. Last year, we expanded our mobile auction network to bring the auction experience directly to dealers' lots. By doing so, we reach underserved markets while helping dealers expand their customer base.

### **Partner for Success with Clients**

Even in a digital world, Manheim believes that building deep, collaborative relationships with clients contributes to new innovations and revenue streams. For example, when Hendrick Automotive Group needed to find a better way to remarket trade-ins, it looked to Manheim to help create its first on-site auction lane. In 2014, we opened Manheim Charleston (S.C.), a one-lane, retrofitted operation to take wholesale trade-in vehicles from Hendrick's 11 area facilities, consolidating its remarketing capabilities and increasing efficiencies. And a year later, Manheim partnered with Hendrick again to establish Manheim Charlotte (Concord, N.C.), a four-lane location that allows Hendrick to more efficiently source and remarket vehicles for its 26 area dealerships. Working with this client, we created a solution that could not have been imagined just a few years ago.

And for more than two decades, the Used Car Market Report itself has been a prime example of our partnership with clients. Using research and expertise found in this report can help clients identify optimal pricing, analyze buying and selling channels, and find inventory in a more coordinated way.

In the year ahead, we're committed to delivering new and better ways to help clients succeed. As we move forward, we invite you to challenge us to further innovate and make changes that truly lead to greater speed and efficiencies—and, ultimately, to your success.

Sincerely,

A handwritten signature in white ink that reads "Janet". The signature is fluid and cursive, written on a blue background.

Janet Barnard  
*President, Manheim North America*

**2016 USED CAR MARKET REPORT**

# **YEAR IN REVIEW AND OUTLOOK**

## 2015 HIGHLIGHTS

The economy added 2.7 million jobs in 2015, bringing the total increase over the past six years to 12.5 million.

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Homeownership rates hit a 48-year low in 2015; since 2006, the number of single-family homes occupied by renters has grown 34 percent, while the number occupied by owners has declined slightly.

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Autos have been a gem in an otherwise dull economy. New unit sales in 2015 were up 68 percent from 2009's trough, and auto loans outstanding grew from \$700 billion in mid-2011 to over \$1.1 trillion today.

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Only three times in the last 61 years has a double-digit increase in new vehicle sales occurred when real GDP was growing less than 3.3 percent. Those three years came consecutively: 2010, 2011 and 2012. Only once have new vehicle sales increased in a year when GDP grew less than 1.5 percent. That year was 2013.

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Dollar appreciation held back multinational profits and manufacturing in the U.S., but not enough to erase overall economic growth. Look for a repeat in 2016.



Whether you're measuring unit sales, revenues, operating efficiency, or profits; whether you're focused on retail or wholesale; or whether you're interested in new or used, it was another good year for the automotive industry. The industry, however, has always been very cyclical (often, harmfully so), so it is only natural to wonder when this pattern will inflect and what the trajectory will be.

The loss of jobs during the Great Recession was stunning. The peak to trough swing in employment was 6.3 percent — that represented a loss of 8.8 million jobs. After steady monthly increases starting in 2009, total employment made it back to its previous peak in May 2014 — and now it is nearly 5 million higher.

All indications are that the good times will continue to roll awhile longer, and even when it rolls over, the descent will be gradual. Why such optimism? From the macro perspective, the slower-than-average recovery has created a more sustainable one. Excesses are not building up. Within the auto industry, we do see growth that is significantly above the overall economy but, here too, no excesses. The auto industry's recovery has been driven by pent-up demand, structural industry shifts, exciting new product, a credit environment that is extremely favorable (but not reckless), and other helpful industry-specific factors. In other words, the growth was earned, not stolen from the future.

To be sure, the overall economy faces several downside risks (any one of which could topple the less-than-robust recovery), but the odds of their happening in 2016 remain relatively low. Before noting those possible threats, let's review the more likely outlook for various forces in the economy.

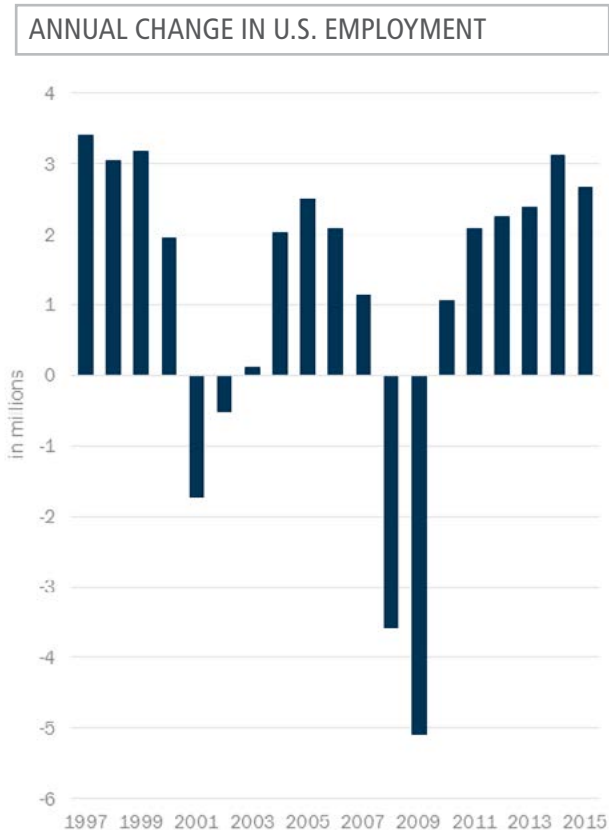
### **"FULL EMPLOYMENT," NOT "ROBUST EMPLOYMENT"**

The economy added 2.7 million jobs in 2015, bringing the total increase over the past six years to 12.5 million. That's a number that just by itself supports the strength of the auto industry. So why haven't things been even better? Because when you combine all of the various labor market metrics, it paints a picture of "full employment," not "robust employment."

Consider, for example, that the labor force participation rate hovers near 40-year lows, wage growth has been mediocre, labor force productivity growth is abysmal, and involuntary part-time work remains high.

The loss of jobs during the Great Recession was stunning. The peak to trough swing in employment was 6.3 percent — that represented a loss of 8.8 million jobs. After steady monthly increases starting in 2009, total employment made it back to its previous peak in May 2014 — and now it is nearly 5 million higher.

Full-time employment, however, didn't get back to its previous peak until October of last year. And, at the start of 2016, the number of people employed full time was basically the same as it was way back in November 2007. Given that, it's not surprising



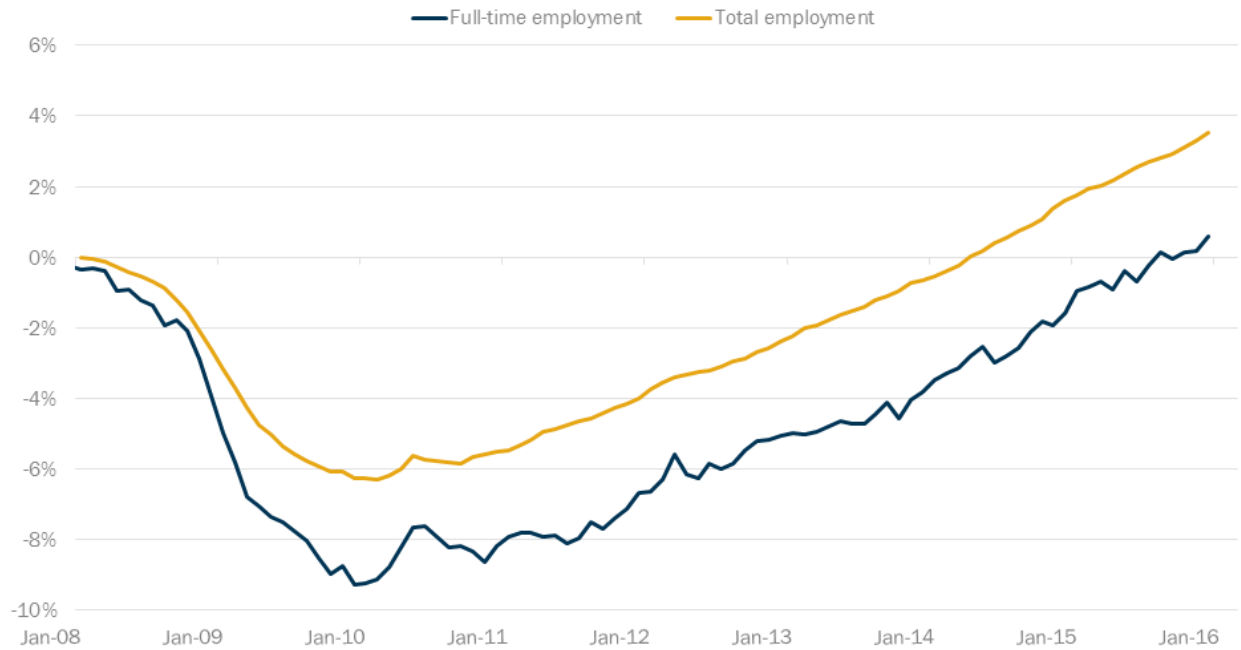
Source: Bureau of Labor Statistics

that the health of the labor market varies as widely as ever with respect to different socioeconomic and demographic groups.

But even though the labor market has been less than robust, it has been exceptionally stable. Witness the steep drop in initial jobless claims. Adjusted for employment, they were at all-time lows throughout

2015. Relatedly, the number of job seekers per job opening also hit a new low in 2015. Those conditions give households the confidence to borrow—and, more important, lenders the willingness to lend. It also creates a virtuous circle where low delinquencies further increase the willingness to lend, which in turn leads to higher spending and a healthy labor market.

PERCENT CHANGE FROM PREVIOUS PEAK



Source: Bureau of Labor Statistics

INITIAL JOBLESS CLAIMS



Source: Bureau of Labor Statistics



### THE FED MAKES ITS MOVE

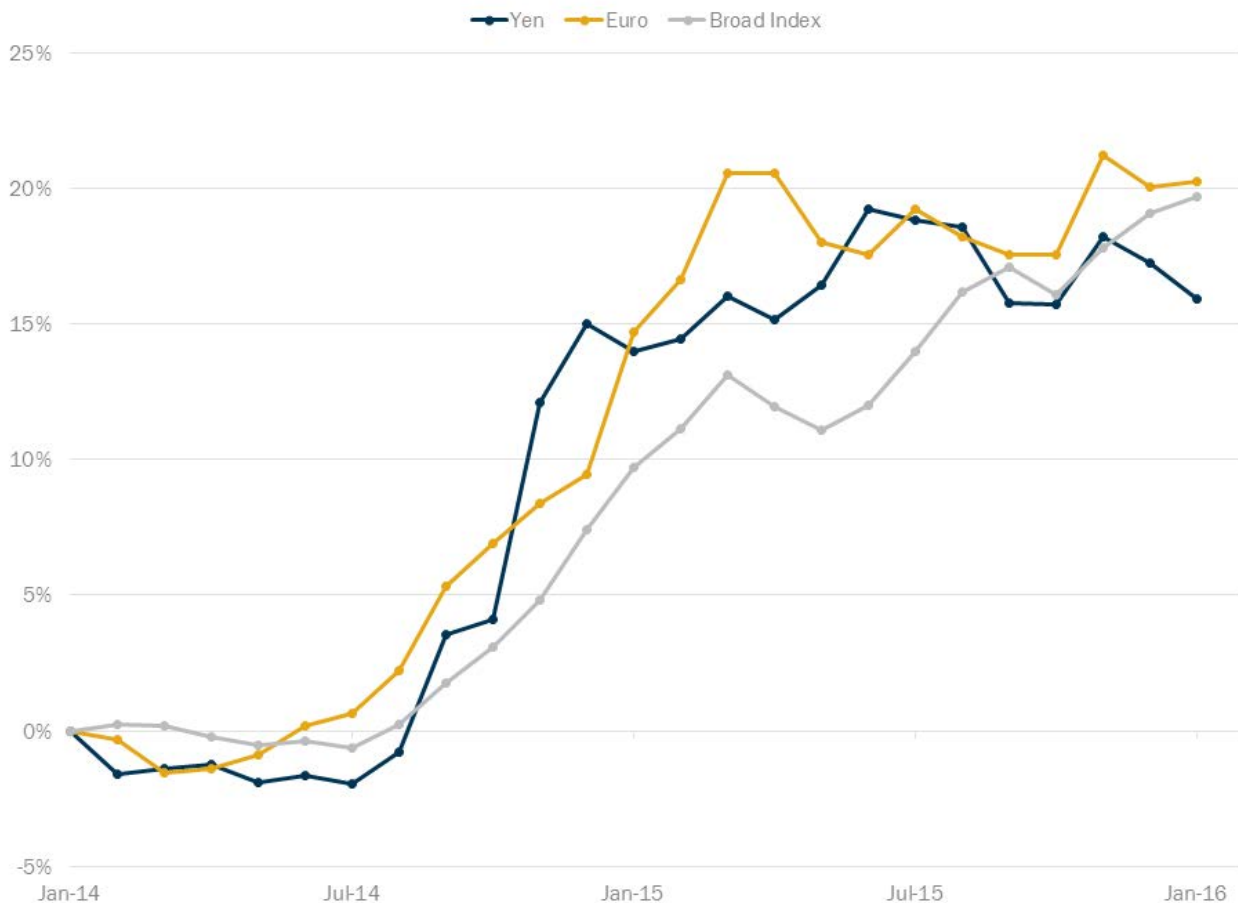
The Federal Reserve hiked the targeted federal funds rate by 25 basis points at its mid-December meeting. (That was later in the year than most analysts were expecting at the start of 2015.) The action (and inaction before that) generated a lot of press coverage, and it is expected that the Fed will make a couple more hikes in 2016; but both the availability and cost of retail credit will remain supportive to the new and used vehicle markets in 2016.

Where we will see the repercussions, if any, will be in exchange rates, international capital flows, high-yield spreads, and possibly a minor headwind to the real estate market. Between September 2014 and March 2015, the U.S. dollar strengthened significantly against the yen, the euro, and a broad basket of international currencies based on the scenario that the Fed would tighten while other central banks eased. With the

Fed's not acting until mid-December, the dollar moved sideways for the remainder of 2015. Now, we have once again introduced the ingredients for another leg up in the dollar and the resulting downside to exports and multinational earnings—not to mention the impact on competitive dynamics in the auto industry. All of those issues are manageable, however.

What is of more concern is the possible volatility in capital flows created by a tightening Fed and easing European Central Bank, Bank of Japan, and People's Bank of China. The market reaction from mid-December to the end of the year was positive. The first week of January, not so much—but there were a lot of other issues in play. Given the sensitivities of global economies, we expect the Fed will err on the side of caution in 2016. Nevertheless, there are several economies around the world that could slip into a severe slide even without outside influences.

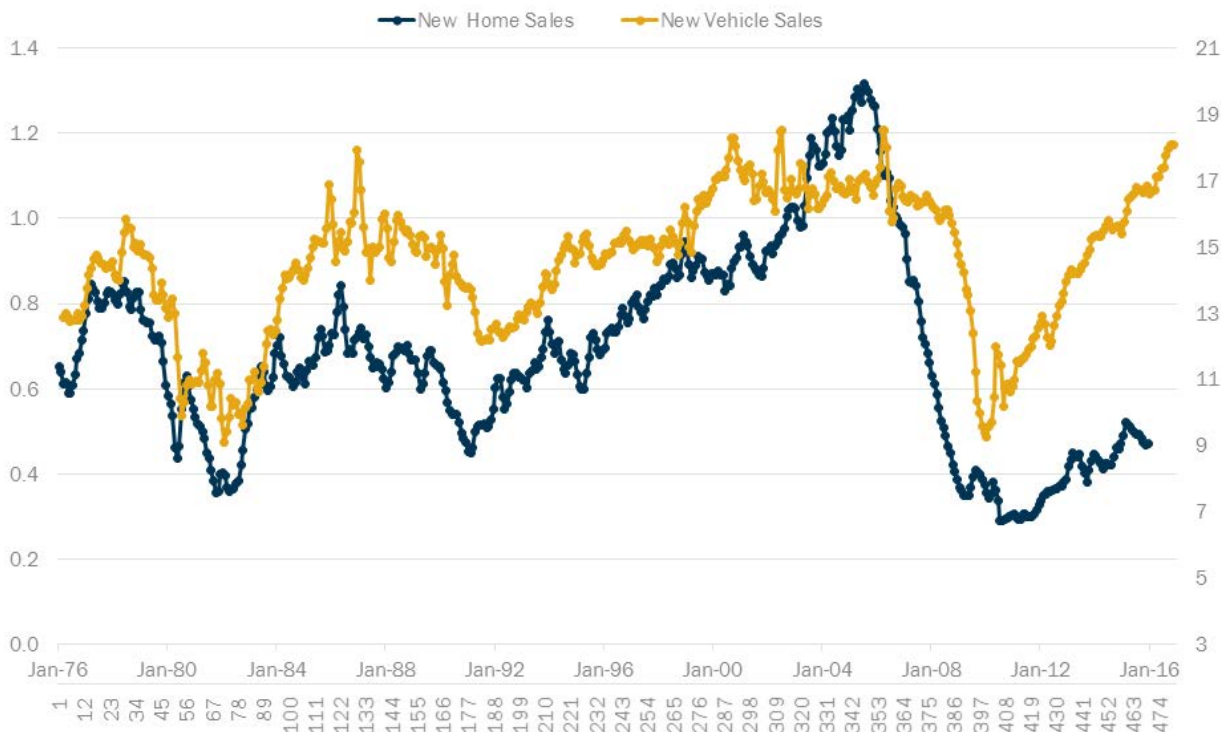
**EXCHANGE RATES**  
PERCENTAGE GAIN IN U.S. DOLLAR FROM JANUARY 2014



Source: Federal Reserve Board

NEW HOME SALES VS. NEW VEHICLE SALES

Seasonally Adjusted Annual Rate—In Millions—3-month average



Source: U.S. Census Bureau

**HOUSING: SOME BENEFITS, BUT UNEVENLY DIVIDED**

The causes and consequences of the Great Recession were concentrated within the housing industry; therefore, it was always expected that the recovery would be measured. It has been. Nevertheless, the improvements in the housing industry have contributed to economic growth and household wealth over the past several years.

Home sales and starts remain well below their pre-recession levels, and the pace of recovery stands in stark contrast to that of autos (an industry that housing used to move in lockstep with); but with home values rising and mortgage obligations still well below their peak, net equity in real estate has risen by more than \$6 trillion over the past four years and owners’ equity as a percent of value has returned to pre-recession levels.

Unfortunately, that equity growth has only widened the inequality of income and wealth in the U.S.—an issue that is now so pronounced that it promises to stifle future growth. Homeownership rates hit a 48-year low in 2015. Since 2006, the number of single-family homes occupied by renters has grown 34 percent, while the number occupied by owners has declined slightly. Thus, the benefits of real estate price appreciation will not flow to many in the middle class. It is true that over-

investment and mal-investment in real estate destroyed the finances of many households in the last cycle; but over the longer term, homeownership has served as a safe, leveraged investment and retirement vehicle for a population that saves too little. Additionally, rapidly rising rents have led to a significant, and growing, number of households that have excessively high rent-to-income ratios. That is not the sort of thing that will lead to a robust new and used car market in the future.

The future course of housing will be a major determinant of the economy’s strength since the contribution from autos has probably peaked. And what that course will be is totally unclear. Optimists point to the large number of millennials who will be entering (or have postponed) their household formation stage in coming years, but this may simply lead to more multifamily construction (already at a 30-year high) and more renting of single-family homes. Those forces add to economic growth, but they do not drive household wealth for the younger generation or spread that wealth more evenly.

It is also uncertain what the impact of higher mortgage rates, and no easing in lending standards, will have on the ability of first-time homebuyers (a group largely absent to date) to jump-start housing. It is clear, however, that the benefits of refinancings are over. Over the past five years, there were over 23 million home refinancings.

OWNERS' EQUITY AS % OF REAL ESTATE VALUE



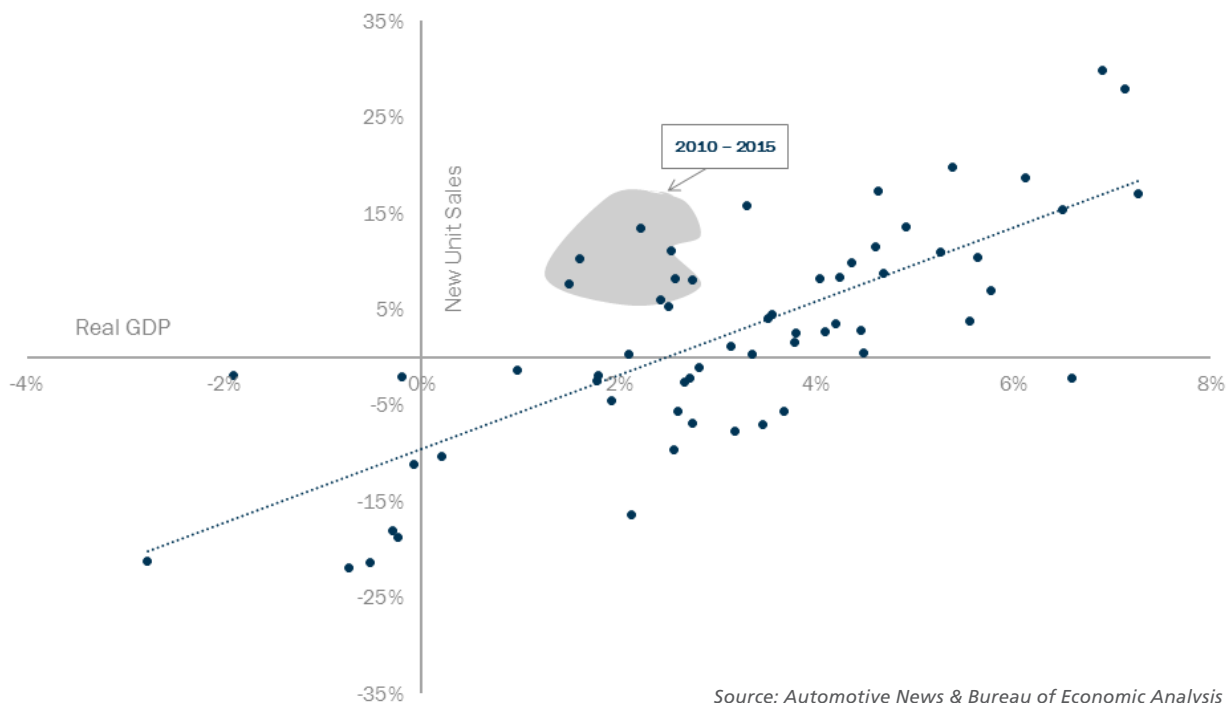
Source: Federal Reserve Board

**AUTO INDUSTRY CONTINUES TO OUTPERFORM THE OVERALL ECONOMY**

Autos have clearly been a gem in an otherwise dull economy. New unit sales in 2015 were up 68 percent from 2009's trough, and auto loans outstanding grew from \$700 billion in mid-2011 to over \$1.1 trillion today. This outsized growth in the auto industry defied the historic relationship between new vehicle sales and overall economic growth.

In the graph presented here, each dot represents one of the 61 years between 1955 and 2015. The x-axis shows the annual percent change in real GDP for that year, and the y-axis is the percent change in new vehicle sales. Naturally, there is a strong correlation. And naturally, there will be outliers since it is based on simple annual percent changes.

CHANGE IN NEW UNIT SALES VS. CHANGE IN REAL GDP: 1955-2015



Source: Automotive News & Bureau of Economic Analysis

*So how strange have the past six years been?*

*Consider this:*

- Only three times in the past 61 years has a double-digit increase in new vehicle sales occurred when real GDP was growing less than 3.3 percent. Those three years came consecutively: 2010, 2011, and 2012.
- Only once have new vehicle sales increased in a year when GDP grew less than 1.5 percent. That year was 2013.
- 2014 and 2015 were closer to the trend line, but still above it for the sixth consecutive year.

## **A WORLD CONNECTED BY CAPITAL AND CONFLICT**

We ended last year's Review and Outlook with the same subhead as above. It certainly wasn't the most profound of statements, but it was prescient. Significant terrorist events showed their ugly heads at both the beginning and end of the year, and many of the months in between. The capital conflict in 2015 was more erosion than explosion. Dollar appreciation held back multinational profits and manufacturing in the U.S., but not enough to erase overall economic growth. Look for a repeat in 2016.

Export/import activity as a share of GDP is considerably less for the U.S. than for other major developed countries, but that simple accounting doesn't capture the critical importance of international capital flows or the dollar's role as the world's reserve currency. Our financial markets are not immune to foreign economic forces, and those outside influences will likely remain negative in 2016 as many of the other major world economies slow and as other foreign central banks pursue policy that is opposite of our own Federal Reserve's.

To the automotive ecosystem (manufacturers, dealers, lenders, and the many other auto-centered industries), we offer the same advice as last year: "Pursue aggressive innovation, but avoid the temptation to force growth."

**2016 USED CAR MARKET REPORT**

# **REMARKETING INDUSTRY OVERVIEW**

## 2015 HIGHLIGHTS

The National Auto Auction Association estimates that member auction sales rose 6 percent to 9.3 million units in 2015.

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Wholesale prices (mix-, mileage-, and seasonally adjusted) increased in both 2014 and 2015 on an average annual basis, and they have been in an elevated range for six years.

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Statistically speaking, the last four years have shown the least volatility in wholesale pricing since the Manheim Index's inception in 1995. At year's end, wholesale prices were only 1.6 percent below the all-time high reached in May 2011.

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For most dealers, auction cars make up 30 percent or more of their used vehicle inventory. To maximize profitability, dealers must be increasingly efficient, precise, and sophisticated in order to pinpoint the vehicles they need and bring them home on the money, time and time again.

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Given the increase in commercial consignment sales in 2015 (especially off-lease units), average mileage for vehicles sold at auction fell to its lowest level since April 2002.



## WHOLESALE VOLUMES CONTINUE TO GROW

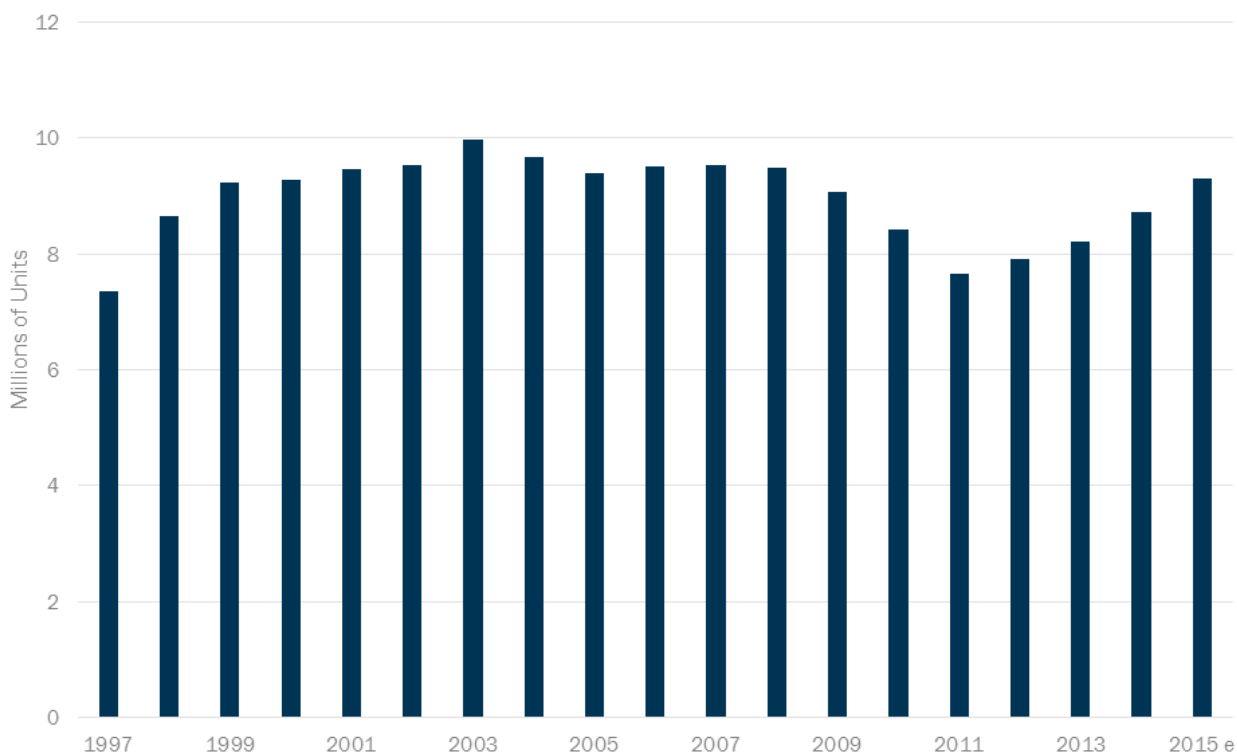
The National Auto Auction Association estimates that member auction sales rose 6 percent to 9.3 million units in 2015. (The final tally will be reported in the first quarter of 2016.) The association further forecasts that volumes will continue to grow in 2016 and 2017 as increased retail activity drives dealer consignment higher and past growth in new lease originations, finance contracts outstanding, and business fleet purchases push commercial consignments up.

Total wholesale transactions in a given year are more than twice the NAAA-member volume. Other channels

include direct sales between dealers (sometimes with a wholesaler as an intermediary), commercial accounts selling directly to dealers or retail customers, and non-NAAA-member auctions. Despite the large volume in the other channels, it is the real-time, competitive-bid, price discovery in the auction channel that serves as the benchmark for pricing in the other venues.

The individual chapters of this report will detail the future volume and remarketing challenges in the various consignor segments. Clearly, however, the biggest growth in wholesale supplies in future years will come from off-lease units.

### NAAA-MEMBER AUCTION VOLUMES



Source: NAAA annual survey

## VEHICLE TRANSPORT

While wholesale volumes have increased to record highs, the growth of vehicle carriers has not kept pace. Logistics and transportation services providers such as the recently rebranded Ready Logistics (formerly Ready Auto Transport) have responded by introducing new efficiencies to their operations in order to meet delivery deadlines for consignors and buying dealers. Performance-based metrics have driven these improvements, while millions of dollars invested in new technology have led to automated processes that minimize costs and speed days-to-delivery. With 70 percent of the transport industry made up of owner-operators, tools developed by companies such as Ready Logistics have improved these small businesses' bottom lines.

## REMARKETING VOLUMES IN 2015

(In millions of units)	Total Wholesale Supply	To Auction (includes online, offsite auctions not to grounding dealer and non-NAAA-member auctions)	Auction Share
Dealer wholesale units	13.29	6.13	46.1%
Off-rental units	1.66	0.89	53.8%
Off-lease units	2.55	1.20	47.0%
Repossessions	1.60	1.29	81.0%
Other*	1.41	0.70	50.0%
<b>Total</b>	<b>20.51</b>	<b>10.22</b>	<b>49.8%</b>

\*Other includes commercial and government fleet, company cars, and some Canadian vehicles

Source: Manheim Consulting

### WHOLESALE PRICING REMAINS STRONG

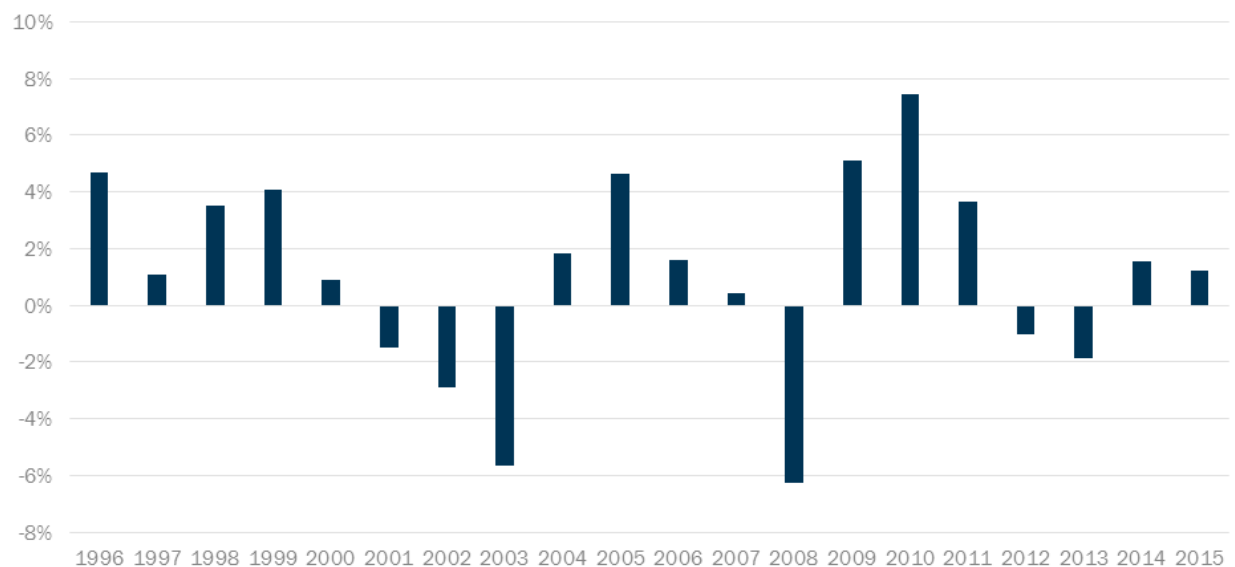
Wholesale prices (mix-, mileage-, and seasonally adjusted) increased in both 2014 and 2015 on an average annual basis, and they have been in an elevated range for six years. Clearly, 2015's upward price movement defied market expectations (as analysts expected higher wholesale volumes would push prices lower), but the price rise did not defy market realities. Indeed, the increase in wholesale pricing reflected the record retail profit opportunities available to dealers in 2015. These record profits and near-record wholesale prices were the result of strong new vehicle pricing,

exceptional credit conditions, higher employment levels, record job stability, and the often overlooked factor of increased dealership operating efficiencies.

Statistically speaking, the last four years have shown the least volatility in wholesale vehicle pricing since the Manheim Index's inception in 1995. A lot of macro-economic and industry factors contributed to that stability; but also give credit to better and more efficient remarketing practices, which enabled commercial consignors to anticipate, respond to, and thus minimize impending swings in wholesale pricing.

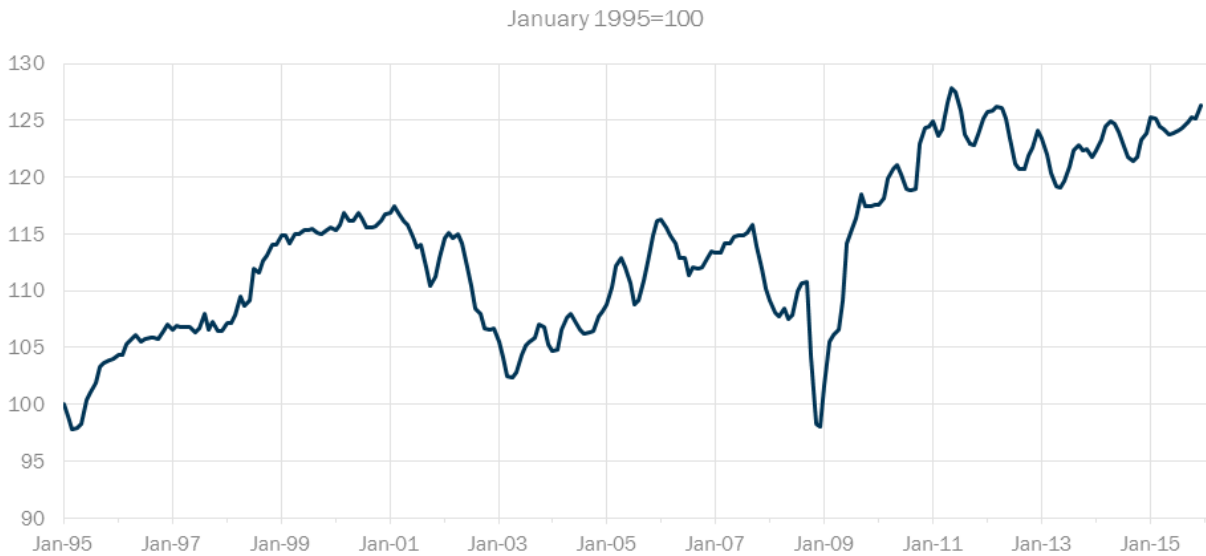
### MANHEIM USED VEHICLE VALUE INDEX

% CHANGE ON ANNUAL AVERAGE BASIS



Source: Manheim Consulting

## MANHEIM USED VEHICLE VALUE INDEX BY MONTH



Source: Manheim Consulting

### FINANCING

With vehicle sales continuing to rise in 2015, financing operations such as NextGear Capital saw unprecedented growth. In NextGear's case, more than 21,000 dealers borrowed from the company in 2015 to acquire inventory. As in other areas of the industry, enhancing speed and efficiency were critical to increased customer satisfaction. Technology improvements, including mobile platforms, allow customers to apply for, and receive, credit more quickly than ever, while customer service call-times are at record lows as teams communicate with dealers in real time (via phone, chat, email, and text). Continued international expansion will be key for NextGear in 2016, building on quick and efficient entries into England and Ireland last year.

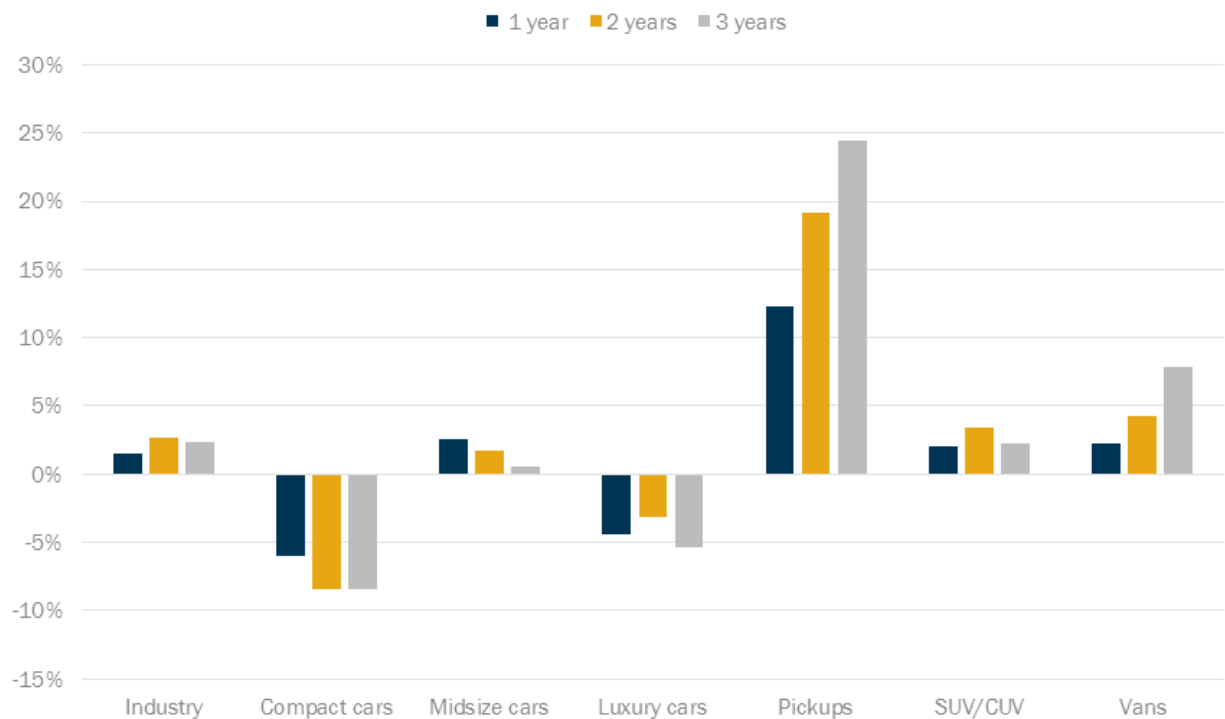
Wholesale pricing started 2015 strong with a significant increase in January, but then declined through May as the spring market provided a less-than-normal bounce for dealers. In the second half of the year, however, dealers posted quick inventory turns and reduced SG&A expenses. As a result, they were more comfortable with bidding up prices at auction. Wholesale prices dipped in November, but they rose again in December. At year's end, wholesale prices were only 1.6 percent below the all-time high reached in May 2011.

### PICKUP PRICES KEEP RISING

Wholesale pricing for used pickup trucks has been especially strong in recent years as a result of higher pricing in the new truck market, greater demand created by construction activity, low gas and diesel prices, and a wholesale supply that has grown more slowly than some other vehicle segments. On a mileage-adjusted basis, pickup prices have risen nearly 25 percent over the past three years.

Compact cars have significantly underperformed the overall market due to fierce price competition on the new vehicle side and shifting consumer preferences. That segment was down over 5 percent in just the past year and 8.4 percent over the past three years.

**PERCENT CHANGE IN WHOLESALE PRICES FOR SELECTIVE MARKET SEGMENTS**



Source: Bureau of Labor Statistics

**AGE AND MILEAGE SHIFTS FOR AUCTION SALES IN 2015**

Given the increase in commercial consignment sales in 2015 (especially off-lease units), average mileage for vehicles sold at auction fell to its lowest level since April 2011. And even the mileage of dealer-consigned

units fell in 2015 as dealers received newer trade-ins. Still, with the average age of a vehicle in operation remaining above 11 years and with total vehicle miles of travel accelerating in the back half 2015, look for the average age and mileage of vehicles sold at auction to remain high.

**INDUSTRY DISRUPTORS**

The used car industry experienced disruptive activity in both the retail and wholesale markets in 2015, primarily related to digital technologies. On the retail side, “omni-channel” selling gained increased traction as even the largest retailers supplemented their traditional offerings with online tools to facilitate the transaction process. For example, customers may have researched and haggled over price online before coming into the dealership to test-drive and purchase the vehicle at an already agreed-upon price. Others, such as MakeMyDeal and Carvana, offer a near online-only buying experience for the customer. From a wholesale perspective, there continued to be increased use of digital channels—in both open and closed selling environments—by OEMs and their captive finance arms. Two other developments to watch: as ride-sharing (Uber, Lyft) continues its ascent, including major investments by manufacturers, will higher utilization of vehicles lead to a fleet-like ownership model in the industry? And how will volatility in international economies impact the inventory supply of U.S. manufacturers?

## FOUR WAYS DEALERS SUCCEED SOURCING INVENTORY AT AUCTION

For most dealers, auction cars make up 30 percent or more of their used vehicle inventory. To maximize profitability, dealers must be increasingly efficient, precise, and sophisticated in order to pinpoint the vehicles they need and bring them home on the money, time and time again.

- 1. Know exactly what to buy.** It's impossible, without the help of technology and tools, to know how a specific vehicle's color, equipment, mileage, ownership history, and trim level will play against competing cars. Dealers who reinvent their acquisition strategies use this car-specific precision to build auction shopping lists that include alternative choices if they can't get the cars they want the most.
- 2. Know where to buy.** With increased competition to acquire auction cars, many dealers recognize they need to expand their sourcing efforts beyond the local auction. The most proficient dealers and buyers rely on technology to tell them where the cars they want reside and to facilitate the transfer of the purchased units back to the dealership. The end result: They are more efficient and productive buyers every time they go to an auction to supplement their inventories.
- 3. Buy at the right price.** Dealers who reinvent their auction sourcing efforts eliminate the guesswork that once guided their bidding on auction cars. Today, they know the maximum they can afford to pay on every vehicle by using technology and tools to calculate each unit's profit potential (accounting for the costs of acquisition, transportation, reconditioning, etc.) before they make a first bid.
- 4. Do it all faster.** With technology, dealers and used vehicle managers can prepare for auctions in minutes, not hours. They eliminate trips to auctions where the cars they need weren't there in the first place. They waste no time bidding on the wrong cars.

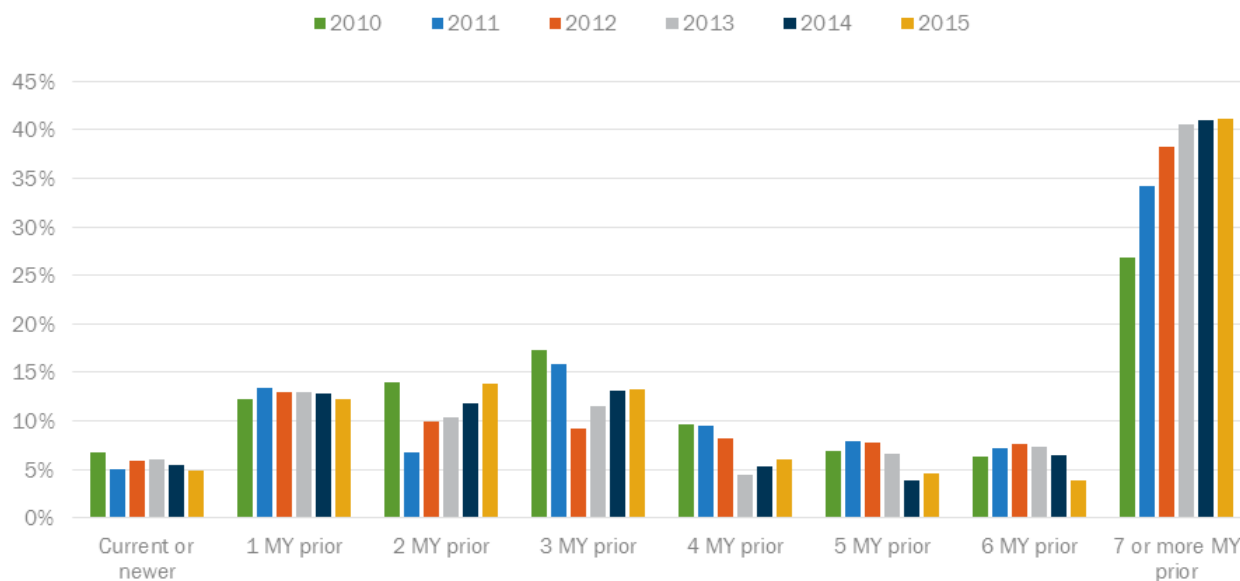


Dale Pollak

The good news for all dealers is that the effort needed to achieve these operational imperatives won't be as daunting as they may seem. vAuto, for example, is developing a technology solution that, almost with the flip of a switch, will soon help dealers gain a higher level of auction sourcing efficiency and proficiency than previously possible.

*Excerpted from Dale Pollak column in Used Car News*

## PERCENT DISTRIBUTION OF AUCTION SALES BY MODEL YEAR



Source: Manheim Consulting

The model year distribution of vehicles sold at auction reflected these same trends. The share of sales accounted for by vehicles from two and three model years past hit a cyclical low as a result of low off-lease volumes in 2011 and 2012. The share of sales accounted for by these relatively new used units rose in 2015. Nevertheless, the share of sales accounted for by vehicles from seven or more model years past remained high at around 40 percent.

### BUYERS HAVE MORE OPPORTUNITIES AND MORE CHALLENGES

Today, dealers have access to millions of vehicles every single day across numerous buying channels. While this means abundant inventory opportunities exist, these options are potentially harder to sort through. For example, expanding the buying radius allows access to more vehicles, but it becomes critical to narrow the focus to specific inventory needs. So how are the most successful dealers sourcing and selecting inventory? Finding the right car, for the right price, in the right place, can only be accomplished with the right tools.

#### How are dealers finding the right cars?

The savviest dealers take advantage of cutting-edge technology to make it easier and faster to find inventory. Online search tools quickly isolate and highlight inventory based on the buyer's most often searched vehicles and buying patterns. Search recommendations allow a dealer's most sought after vehicles to be "pushed" to the top of a search list, allowing the inventory to "find them first."

Dealers need all the critical vehicle information readily available and easily accessible to react quickly. Time

can't be wasted sorting through multiple sources. Dealers should expect the most valuable vehicle information aggregated in one place that provides a consistent and relevant decision-making experience. It's not just about having more information; it's about having more information delivered in a way that speeds up the decision-making process.

Once the ideal car becomes available, it's critical that buyers act quickly before the opportunity is lost to a competitor. Dealers no longer have the luxury of waiting until they sign in online or arrive at an auction to begin the purchase process. Mobile text notifications alert buyers immediately to an opportunity no matter where they are and allow them to respond in minutes, reducing the time to close an important deal.

Additionally, proxy bidding has traditionally allowed buyers to set automatic buying parameters to purchase the right vehicle when they can't bid in person. This meant never allowing a good opportunity to pass by. Enhancements to that capability will soon allow dealers to not only get the right car, but to get the right cars in the exact volume that they need by using predefined rules to cut off bidding when a certain threshold is met. This will rapidly expand buying power, allowing dealers to purchase more vehicles in less time—but only for targeted inventory.

What happens when a buyer has done all the right things, but still ends up with the wrong vehicle? Purchase protection is critical for dealers to feel confident when making purchase decisions. Major opportunities may be missed without that peace of mind. Dealers have the flexibility—before and after



## ASSURANCE

With the rise of online sales activity, the concept of “assurance” in the wholesale marketplace has taken on increased visibility and importance. Whether through the ability to access Condition Reports with High Resolution Images of the vehicle, detailed inspections either prior to the auction or post-sales or a pure guarantee of quality without an inspection, such as the DealShield product, dealers are seeking the peace of mind that comes with buying with confidence. No longer do dealers need to be concerned about mechanical or cosmetic issues that may have gone undetected. Instead, they can focus on acquiring the right, front-line ready inventory for their lots—making the wholesale-to-retail cycle quicker than ever.

the purchase—to back out of a vehicle acquisition with offerings such as a sale day inspection, post-sale inspection, and buy-back guarantees.

### *How are dealers finding vehicles at the right price?*

Dealers have long used industry valuation tools such as Manheim Market Report (MMR), NADA, Kelley Blue Book (KBB), Black Book, and others to make an informed decision on purchase price. These sources continue to have value and remain an integral piece of the purchase decision, yet dealers always ask for more detailed information to better support buying decisions. As the capabilities of these tools improve, dealers will be able to adjust for color and condition to receive an even more accurate valuation. Local market supply/demand dynamics will also be incorporated to ensure it is the right price for that particular dealer.

### *How are dealers finding vehicles in the right place?*

As the used vehicle marketplace expands, it’s easier than ever to access the same inventory multiple ways—standing in the lane at an auction, on a mobile device, or from a computer. Dealers may prefer to search for vehicles on their desktop yet access the saved search from their mobile phone when they arrive at the auction to bid in person. Dealers want choices for doing business, but it should be a similar experience regardless of which way they choose. Technology and design improvements will make it effortless to move throughout channels seamlessly in a way that looks and feels the same.

Research shows that some dealers prefer to do business closer to home with trusted sellers with whom they have an established relationship. The growth of Manheim Mobile Auctions, with a 22 percent increase in the number of vehicles sold in the last two years, highlights that. Through these mobile sales, the full auction experience is transported to a local seller’s lot including an auctioneer, a single auction lane with cars

driven through, and simulcast broadcasting to online buyers. The smaller setting offers a more personalized experience for in-lane buyers and additional inventory selection for all online buyers through simulcast technology. Manheim currently hosts more than 29 mobile auction sales each month, with more than 100 dealers typically showing up at each sale.

Additionally, competitive transportation options allow dealers to extend their inventory reach to more locations without sacrificing profit margin. It’s not just the cost of transportation but also the time it takes to get the vehicle to the retail lot that is a consideration.

Many strategies exist for dealers when it comes to sourcing and selecting wholesale inventory. Finding the right car, for the right price, in the right place sounds simple but can be executed in countless ways with various tools. Adopting technology, using tried and true valuation tools, and conducting business in a way that works best for dealers (whether that is inlane at the auction or online) will ultimately save time and money. This will improve the efficiency of both the wholesale and retail used vehicle market.

## SELLERS RESPOND TO THE NEEDS OF BUYERS

Looking at inventory disposition from the seller’s perspective, there are similar challenges. An increased market supply makes it difficult to sell vehicles quickly and profitably. Additionally, the continued rise in off-lease volumes makes it essential to move inventory faster than the competition. Fortunately, there are many tools and services that sellers in the wholesale market can rely on to give them an advantage.

One such tool relates to vehicle images and detailed information that allows dealers to clearly and quickly assess what is wrong, or special, about a vehicle and provide greater confidence when buying. Manheim released Enhanced Vehicle Imaging in 2014, providing the highest-resolution vehicle images available coupled with ‘heat map’ graphics that help buyers quickly

evaluate vehicle condition, both of which are offered together within a Manheim Insight Condition Report.

In a recent study conducted in partnership with Toyota Financial Services, Manheim reported that including high-resolution images improved buyers' confidence in Manheim condition reports by 18 percent. The same study showed a 26 percent gain in the number of bids per sale and conversion rates that were 17 percent higher. Condition reports, coupled with high-resolution images, provide additional trust in the purchase decision for the buyer—and that translates into more sales.

Sellers are always looking for more exposure and greater visibility for their inventory to potential buyers. Future online enhancements will allow for a vehicle scheduled for a sale at a later date to appear in a buyer's current search results. A motivated buyer would then have the option to immediately make an offer or buy now at the seller's list price instead of waiting for sale day. This continuous inventory availability capability not only means more eyes on cars, but also more exposure outside of sale day for sellers. Buyers benefit from getting the car faster, and sellers are able to remarket inventory quicker. It's a win-win.

Selling more cars also means dealers have to make more complex decisions. If the majority of vehicles in a sale are sold, a dealer may choose to hold out for a higher offer on the remaining vehicles to increase overall revenue. Or if overall revenue is up, a dealer may be willing to take a

little less on one car to make the sale of another happen and avoid transportation costs back to the lot. The key is having all the information to make the best decisions, not only about a single vehicle, but holistically across the entire offered portfolio. Near-term advances will allow sellers one view of all registered vehicles through an interactive dashboard that provides sale day and historical information along with a valuation calculator. This will enable dealers to make educated decisions that ultimately lead to increased conversion rates.

Time becomes more limited with the increasing pressure to sell more quickly and for a higher profit. Too often that means being spread thin across business functions. Sellers are increasingly relying on third-party partners to take over some aspects of the business such as reconditioning, detailing, imaging, and transportation. Trusted and experienced partners will allow them to focus on the core business of selling cars. This approach allows dealers to invest in the strengths that differentiate them, creating a sustainable competitive advantage.

In 2016, time, tools, and educated decision-making across one's business will remain critical for sellers. Sellers will need to continue to rely on up-to-date industry tools and services to allow them to focus on the core business, thus impacting the bottom line of their businesses.

## INSPECTIONS AND FRONT-LINE READY VEHICLES

For more than 70 years, Manheim has provided reconditioning and repair work for vehicles for sale at auction. Today, Manheim has expanded the value it extends to dealers by providing similar services for vehicle buyers beyond the auction. Manheim's Retail Services operation delivers front-line ready vehicles, allowing dealers to focus on their customers. For example, a partnership with Sonic Automotive's EchoPark used car stores has Manheim providing reconditioning and mechanical work in Denver and Chicago, while another partnership has Manheim prepping vehicles for retail sale at DriveTime dealerships.

In 2015, Manheim also enhanced its work on the inspection side of the business through a strategic alliance with AiM (Alliance Inspection Management), an investment intended to bring greater quality and consistency to the vehicle inspection process. With an increasing number of transactions migrating online, accurate and consistent inspection information is becoming increasingly important to buyers looking for the best value and sellers looking to move inventory quickly. The alliance is an effort to provide products, services and best practices to efficiently support both wholesale and retail activities. Along the same lines, Manheim is making its patented AutoGrade vehicle condition rating system available to the remarketing industry, providing a new standard of accuracy and consistency.

2016 USED CAR MARKET REPORT

# DEALERS

## 2015 HIGHLIGHTS

In 2015, new vehicle sales increased for an unprecedented sixth straight year, and the total, 17.5 million, was an all-time high.

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Used vehicle sales at franchised dealerships have also increased for six consecutive years.

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Consolidation of dealerships continues; buy/sell activity was at its highest level ever, with 184 transactions involving 444 franchises occurring in the first nine months of 2015.

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Manufacturer certified pre-owned (CPO) vehicle sales totaled a record 2.55 million units in 2015, the fifth straight year in which sales reached a new plateau.

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After reaching a high of nearly 59 percent of all NAAA-member auction sales in 2013, the dealer consignment share dipped to an estimated 56.5 percent in 2015, still high by historical standards.

**BUILDING ON SUCCESS WHILE EMBRACING CHANGE**

It’s hard to believe that only six years ago, automotive retailing was in the depths of the recession—suffering record losses, franchise terminations, and bankruptcies. The survivors have done more than just “live to fight another day.” They have triumphed—establishing an industry that effectively and efficiently meets the needs of today’s customers while maintaining the flexibility, and embracing the innovation, needed to meet the coming transformation in the way cars are bought, sold, and owned.

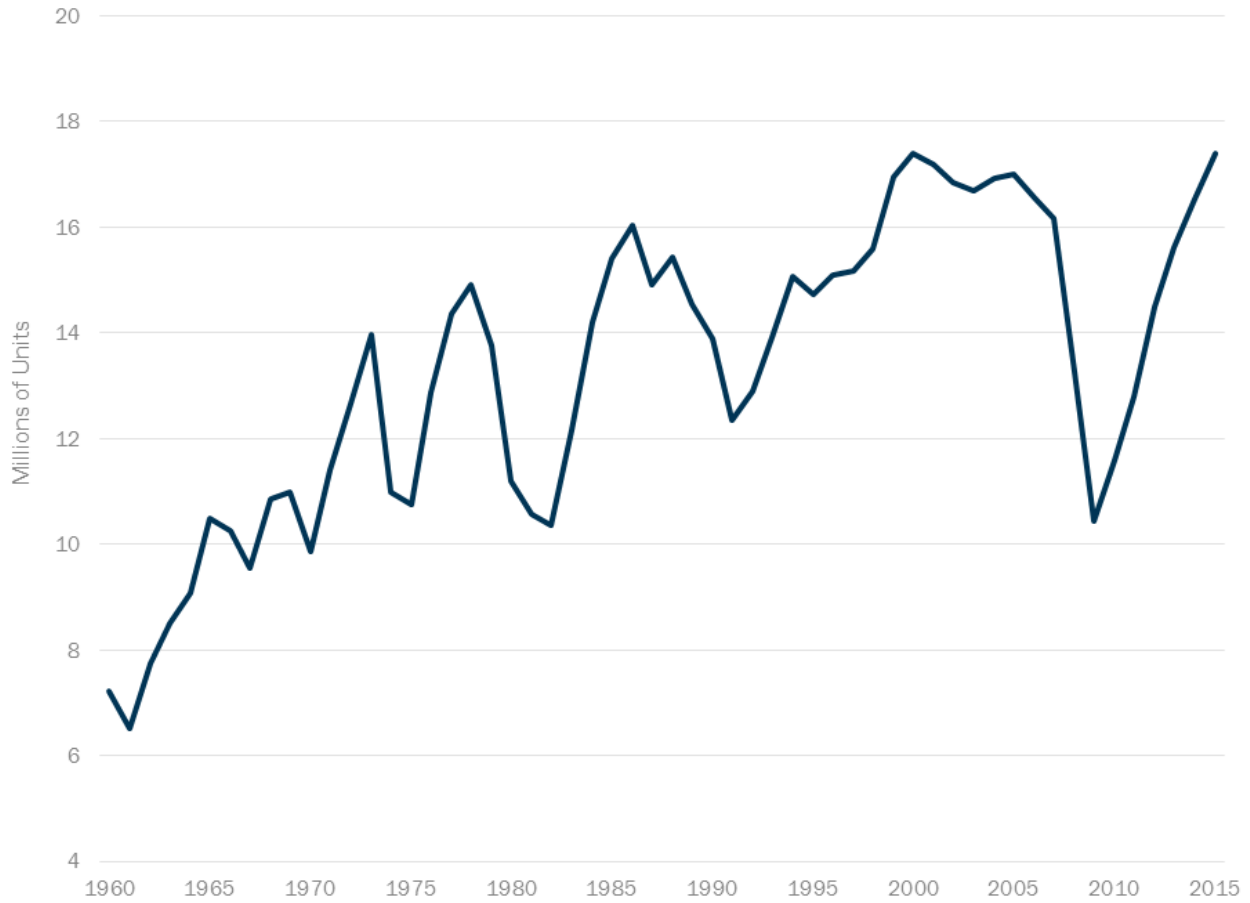
To be sure, automotive retailing is not a monolithic industry, and as such, some segments have not fared as well, or advanced as far, as others. But’s there a common thread for all dealers—when labor market and credit conditions are favorable, it is inevitable that dealers will tap into America’s love affair with the automobile and mobility to create new growth opportunities. Since 2010, jobs and credit availability have been growing, and thus, the success of dealers comes as no surprise.

**FRANCHISED DEALERS GROW SALES, PROFITS, AND THEMSELVES**

**New vehicle sales hit new high.** In 2015, new vehicle sales increased for an unprecedented sixth consecutive year—and the total, 17.5 million, was a record. New vehicle sales have clearly outperformed the overall economy—and one reason is product. Manufacturers are offering quality products with the physical attributes, technology, and features that consumers desire. As a result, customers (aided by attractive finance options) have been willing to pay higher transaction prices and manufacturers have not had to resort to aggressive incentives to meet internal sales projections.

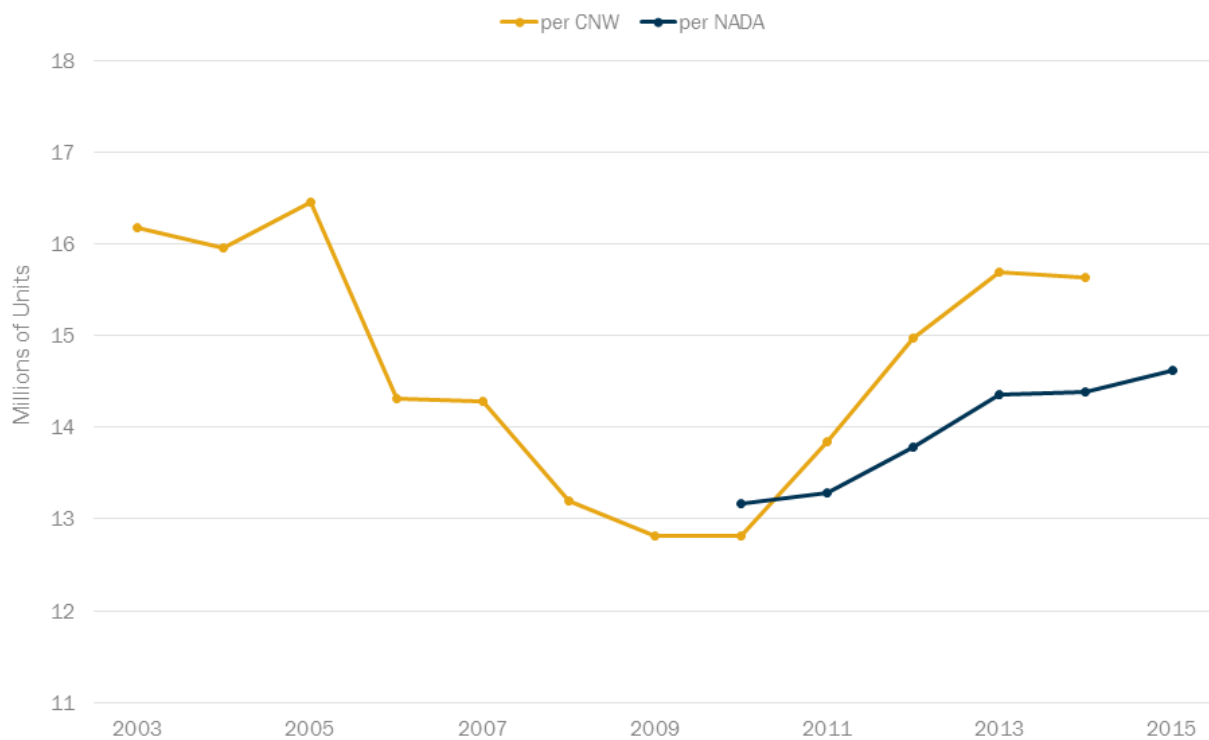
**Used vehicle volumes and profits also rise.** Used vehicle sales at franchised dealerships have also increased six consecutive years, according to NADA. The percentage increases were much smaller than for new vehicles, but that is to be expected for a market that is much more stable over the economic cycle and that declined less than half as much as new vehicles during the recession.

**NEW CAR & LIGHT-DUTY TRUCK SALES**



Source: Automotive News

## USED VEHICLE RETAIL SALES BY FRANCHISED DEALERS



Note: CNW ceased reporting in 2015. NADA started reporting in 2015 using different methodology.

Source: CNW Marketing Research, NADA

Despite narrowing gross margins, used vehicle operations at franchised dealerships produced record profits due to quicker inventory turns, reduced selling expenses, and strong F&I income. In 2016, franchised dealers will benefit from the growing off-lease volumes, which means that quality used vehicle inventory will literally be driven to their door. And that's not to mention that the majority of returning lessees will buy or lease another new vehicle from that dealer.

**Consolidation continues.** Franchised dealership buy/sell activity last year was the most active ever, according to Kerrigan Advisors. They noted 184 buy/sell transactions involving 444 franchises in the first nine months of 2015. After spending \$1.5 billion on acquisitions in 2014, the six publicly traded franchised dealer groups increased outlays another 31 percent in the first nine months. And they weren't the biggest acquirers. That distinction went to the large private dealer groups using their own funds or backed by money from private equity and family offices.

High price-to-earnings ratios for the public groups and a low cost of funds in the capital markets have accelerated the consolidation in automotive retailing. It is also important that manufacturers are now more comfortable with the trend, given that large players and new entrants are making long-term commitments to the manufacturers' brands as well as their own.

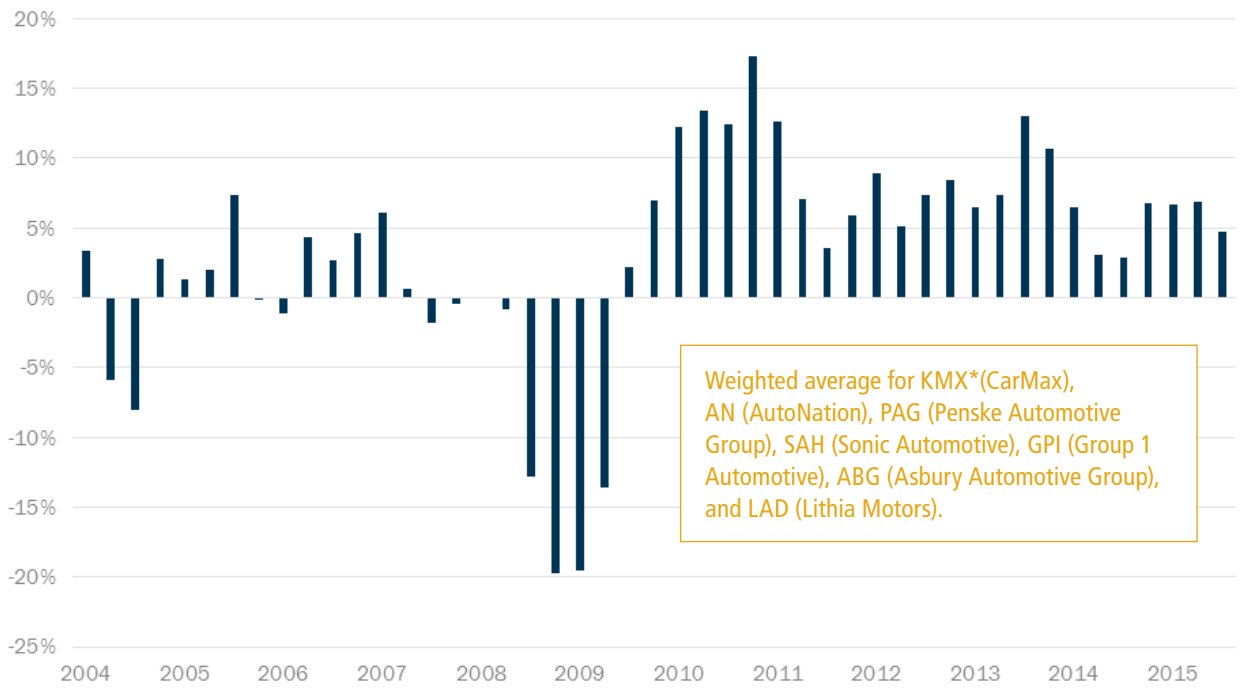
**Dealer groups had another good year.** Financial reports from the seven publicly traded dealership groups provide a good reflection of trends within the franchised dealer body. Yes, the largest of the publicly traded dealers (CarMax) is an independent, but its product offerings and price points are similar to those of a mainstream franchised dealer.

With respect to unit volumes, the trend has been very good. In the third quarter of 2015, the dealer groups posted their 25th consecutive quarterly increase on a same-store basis. The same-store gains in the first nine months of 2015 averaged over 6 percent, and as noted earlier, these dealer groups are also growing through acquisitions. In total, these seven dealership groups retained 1.5 million used units in 2015.

With respect to gross margins, however, the trend is not as pretty. These same dealer groups experienced declining gross margins (on a year-over-year basis) for almost as long. With higher throughput, quicker inventory turns, higher transaction prices, reduced selling expenses, and good F&I income, the reduced margins did not prevent record profits. View the narrower used vehicle margins as a sign of a competitive industry passing on some of its efficiency gains to consumers. The narrowing of margins will, however, present a problem to dealers who have not yet adapted to the changing marketplace.



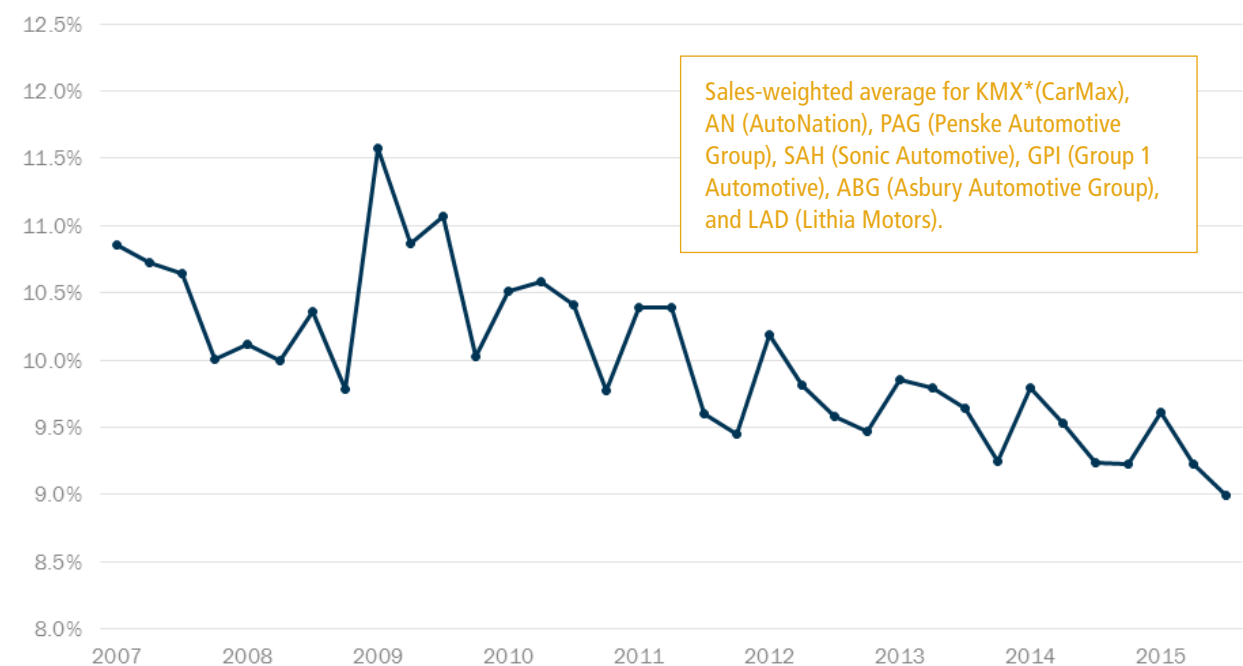
**% CHANGE USED UNITS RETAILED — SAME STORE BASIS**  
PUBLICLY TRADED DEALERSHIP GROUPS



Weighted average for KMX\*(CarMax), AN (AutoNation), PAG (Penske Automotive Group), SAH (Sonic Automotive), GPI (Group 1 Automotive), ABG (Asbury Automotive Group), and LAD (Lithia Motors).

\*KMX shifted forward one month to correspond with calendar quarter Source: Company filings

**USED VEHICLE RETAIL GROSS MARGIN**  
PUBLICLY TRADED DEALERSHIP GROUPS



Sales-weighted average for KMX\*(CarMax), AN (AutoNation), PAG (Penske Automotive Group), SAH (Sonic Automotive), GPI (Group 1 Automotive), ABG (Asbury Automotive Group), and LAD (Lithia Motors).

\*KMX shifted forward one month to correspond with calendar quarter Source: Company filings

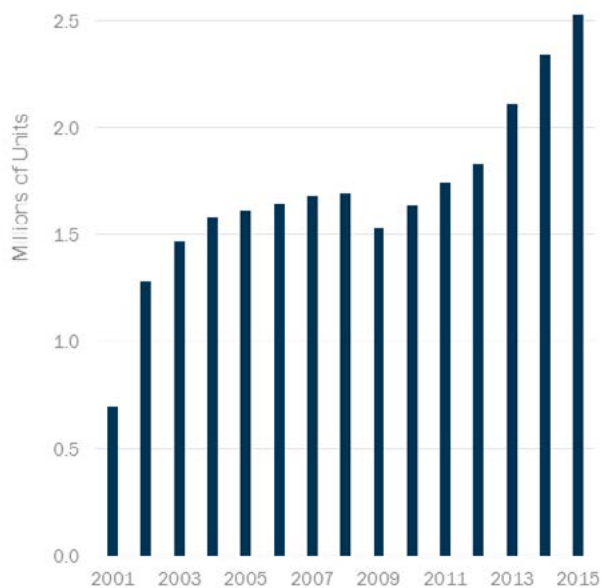
Increased price transparency in the used vehicle market, in addition to narrowing margins, also reduced the range of grosses on individual transactions. Lacking “home-run” (high-gross) deals, dealers can now ill afford the outsized losses associated with buying the wrong car at the wrong price. Hence, the need for dealers to take a more data-driven approach to inventory acquisition. And, for commercial consignors, who often benefited from that one dealer paying too much in a speculative bid, the need for getting their portfolio in front of right buyer—the first time—takes on added importance.

**CPO sales: another year, another record.**

In 2015, sales of manufacturer certified pre-owned (CPO) units totaled a record 2.55 million units. It was the fifth consecutive year in which sales reached a new high, and 2016 promises to be the sixth such year as growing off-lease volumes provide both the need and ability for further growth. There is also the desire to grow CPO sales, since they enable dealers to protect gross margins, improve turn rates, or boost F&I and service income. And, when CPO programs are properly structured and effectively marketed by manufacturers and dealers, the programs can provide all three of those benefits simultaneously.

But, is there a natural limit for future CPO sales? After all, the ratio of CPO sales to the number of new vehicles sold in the prior four years rose from little more than 2 percent a decade ago to more than 4 percent today. And the share of total franchised dealer used vehicle sales that were CPO units rose from 12 percent in 2010 to 17 percent in 2015, according to NADA.

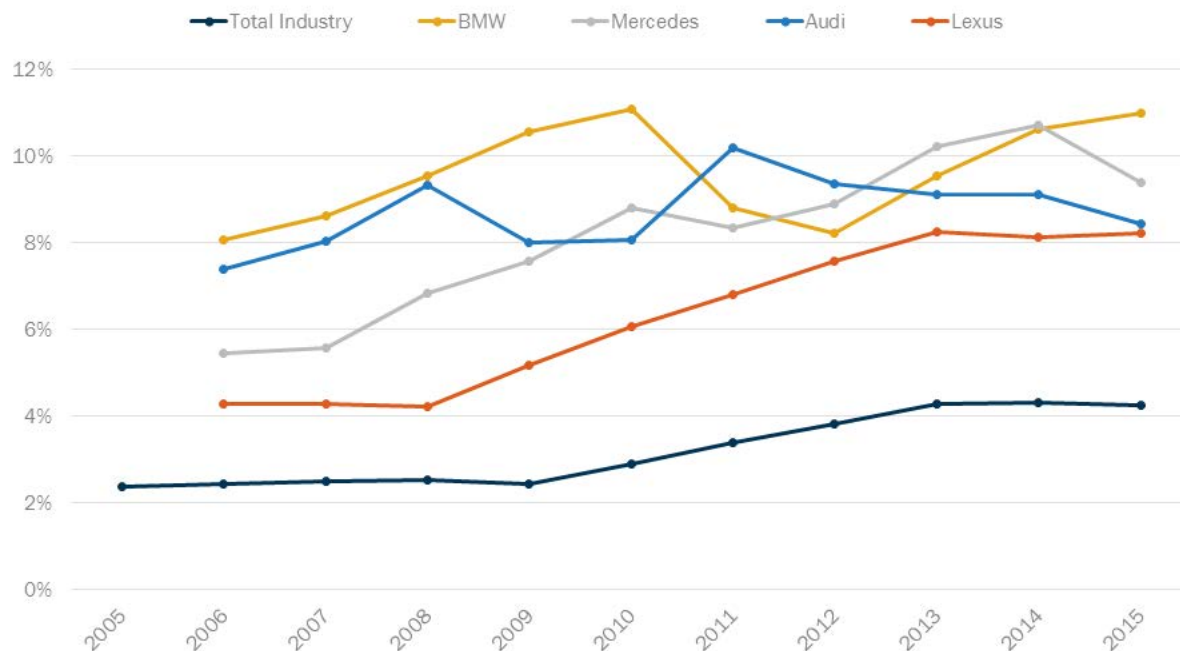
**CERTIFIED PRE-OWNED SALES**



Source: Automotive News

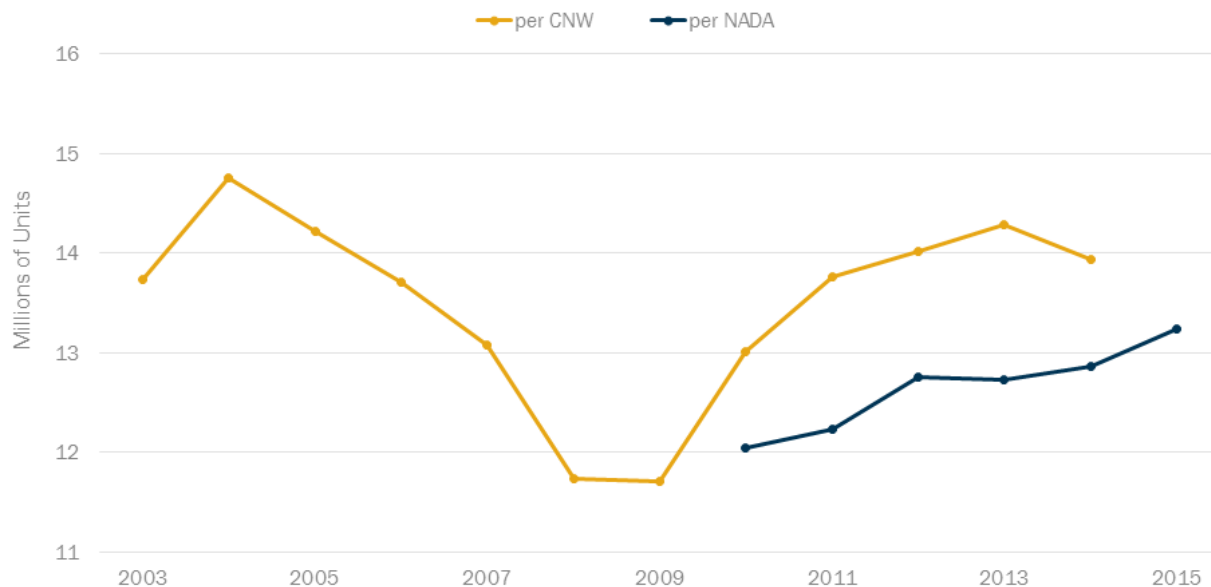
Note, however, that manufacturers that have long-established CPO programs, high lease rates, and remarketing processes that keep a large share of returning units within their dealer network often have CPO-to-prior sales ratios close to double digits. And their dealers often have used vehicle operations where more than half of all used sales are accounted for by CPO vehicles. This means the CPO market has

**CPO AS % OF NEW VEHICLE SALES OVER PRIOR 4 YEARS**



Source: Manheim Consulting

## USED VEHICLE RETAIL SALES BY INDEPENDENT DEALERS



Note: CNW ceased reporting in 2015. NADA started reporting in 2015 using different methodology.

Source: CNW Marketing Research, NADA

at least the potential to continue its rapid growth. It will be a matter of how much marketing muscle the manufacturers want to put behind the programs—and, of course, the dealer's ability to continue to earn good profits on the sales.

### GREATER INVENTORY AVAILABILITY HELPS INDEPENDENT DEALERS

As wholesale supplies grew in 2015, independent dealers were better able to secure inventory that met the needs of their individual customer bases. As a result, unit sales grew considerably faster than in the prior two years, and at a pace that was higher than that of franchised dealers. Earlier in this cycle, many independents suffered as a result of a lower flow of wholesale units from franchised dealers, fewer desirable trade-ins, and reduced auction supplies. With all of those sources' returning to normal volumes, independent dealers should have another good year in 2016, especially if all-important credit conditions remain favorable.

### BHPH DEALERS ADAPT TO CHANGING CONDITIONS

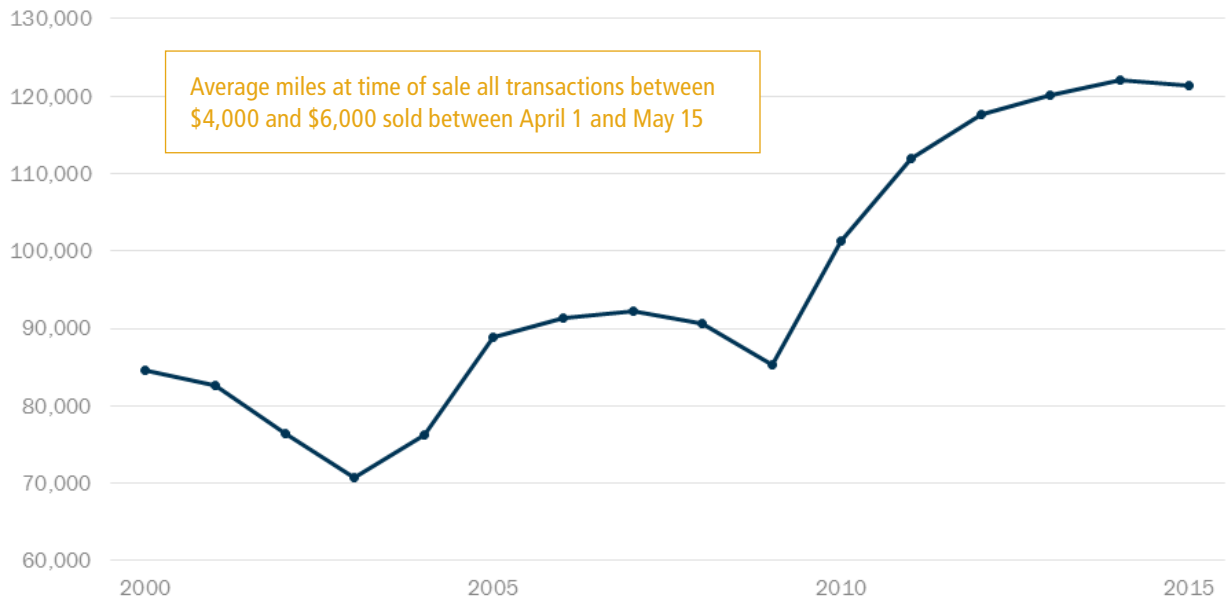
The biggest challenge for Buy-Here, Pay-Here (BHPH) dealers in this cycle has been deep subprime lenders' buying down into the traditional BHPH customer base. The customers left behind were the ones least likely to pay. To handle this and other challenges, individual BHPH operators have developed a multitude of different business models. No longer is there a "traditional BHPH model." Some operators significantly increased the

price point of the vehicles they offer, others kept their price point and built in more goodwill policy work as a reserve, some moved to the Lease-Here, Pay-Here model, others adjusted interest rates to coincide with subprime lenders, and still others worked diligently to capture more upfront money in the deal.

In recent years, many BHPH dealers have used down payment deferral programs to get a jump-start on the tax selling season. And, in 2016, BHPH dealers will also be able to take advantage of the new Tax Refund Advance program that replaces the old Refund Anticipation Loans, which were viewed askance by regulators.

**What \$5,000 will buy.** Rising wholesale prices have often caused headaches for BHPH dealers as they need to find vehicles their customers can afford, but which will also be capable of running the term of the note with minimal repairs. To give a sense of just how much wholesale prices have gone up over time in the lower price tiers, we looked at the average mileage on auction vehicles that sold between \$4,000 and \$6,000 over the past 16 years. As seen in the graphic, if you spent, on average, \$5,000 for a vehicle at auction in 2000, you got, on average, a vehicle with 84,541 miles. Average mileage slipped over the following three years as wholesale supplies grew and the overall pricing environment weakened. But between 2003 and 2014, average mileage for the typical \$5,000 auction purchase rose every year, except for the recession of 2008–2009. In 2015, BHPH dealers got a slight reprieve as the average mileage on a \$5,000 auction purchase dipped, but remained above 120,000 miles.

**WHAT \$5,000 WILL BUY...**



Excludes salvage

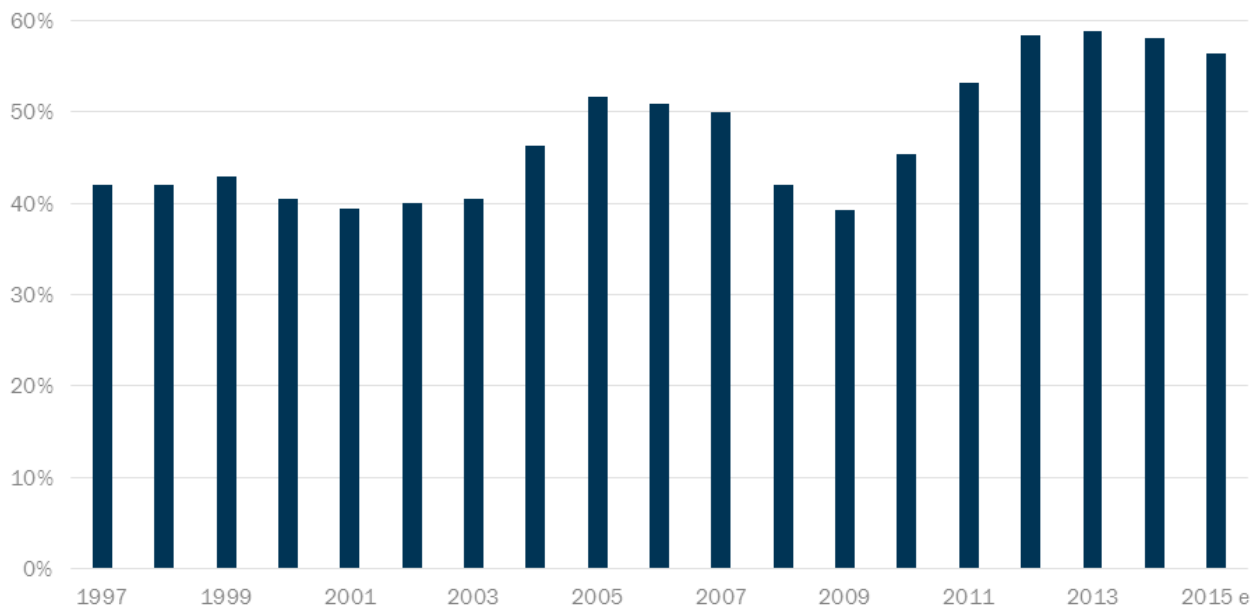
Source: Manheim Consulting

**DEALER CONSIGNMENT REMAINS THE CORE OF AUCTION OPERATIONS**

After reaching a high of nearly 59 percent of all NAAA-member auction sales in 2013, the dealer consignment share slipped to an estimated 56.5 percent in 2015. That's still high by historical standards, and even as

commercial consignments grow more rapidly in the years ahead, it is likely that dealer sales will remain a high and key component of auction volumes. In past cycles, commercial volumes sometimes pushed out dealer consignments due to limited physical capacity, as well as prime lane and time slots. Not so today. Online sales,

**DEALER CONSIGNMENT SALES AS % OF NAAA-MEMBER AUCTION VOLUMES**



\*2015 is a Manheim Consulting estimate based on both internal and industry sources.

Source: National Auto Auction Association Surveys, 2001-2014

multiblock selling, Simulcast, other online options, and mobile auctions have put all sellers on equal footing and have broadened the whole definition as to what a “prime” slot is.

Likewise, several years ago it was argued that traditional auctions would be disintermediated as new and improved online options enabled dealers to more easily bypass the traditional auction process. After all, dealer wholesale transactions outside the traditional auction have always been considerably larger than the number going through auction. And technology was promising to make those informal networks more efficient. What evolved, however, was a stronger partnership between dealers and auctions and the setting up of dealership trade networks that auctions created and play a major role in facilitating.

Going forward, mobile auctions (run by the auction houses) will become an increasingly important method for dealers to sell and source inventory. These auctions enable companies like Manheim to bring the excitement and success of a live auction (coupled with Simulcast

bidding) anywhere and everywhere, typically to a franchised dealer’s lot. Many of these auctions are held in rural areas that are some distance from a major physical auction. Usually the sale is located at the site of the primary selling dealer—and, although the majority of attendees come from nearby areas, there is often robust remote bidding via Simulcast. Manheim has found that conversion rates at these sales are often much higher than for typical physical auction sales because the sellers are very committed. The high conversion rate feeds on itself by attracting more local dealers. Importantly, technology allows Manheim to perform all of the important back office functions and ancillary services just as efficiently as if the sales were held at a major auction house. For sellers, additional advantages include reduced transportation costs, presale marketing by the auction house, and full-service administration of the auction, freeing the dealer to focus on the retail side of his business. Buyers enjoy convenience, cost savings (transportation and time spent traveling to auctions), and an overall “easier” experience with fewer vehicles to track, fewer competitors, and proximity.

## KEYS TO SELLER SUCCESS WITH MOBILE AUCTIONS

- A committed dealer with a solid reputation that will draw enough buyers to make the sale a success for all parties
- A strategy that is appropriate to the needs of the local market. For example, at a mobile sale in Macon, Georgia there are typically 120-150 cars for sale every month. The conversion rate is in the mid-90 percent range. The value of the cars is between \$1,500 and \$3,500. For more than three years, this mobile sale has found its niche selling low-priced cars to area Buy-Here, Pay-Here dealers.
- A minimum of 100 cars per sale, regardless of the frequency (most are weekly or monthly)

### MOBILE AUCTION VOLUME

- Here is a look at the most current data year-over-year:
- Manheim sold 40,000 vehicles through mobile auctions in 2015.
- Currently, Manheim has 29 mobile auctions, with 28 under development. Mobile auctions provide dealers with sales options beyond Manheim’s physical network, and serve smaller markets by reducing transportation expenses and expanding the buying customer base.
- Sales conversion at mobile auctions averages 73 percent across all Manheim, the highest across any of the company’s sales channels.

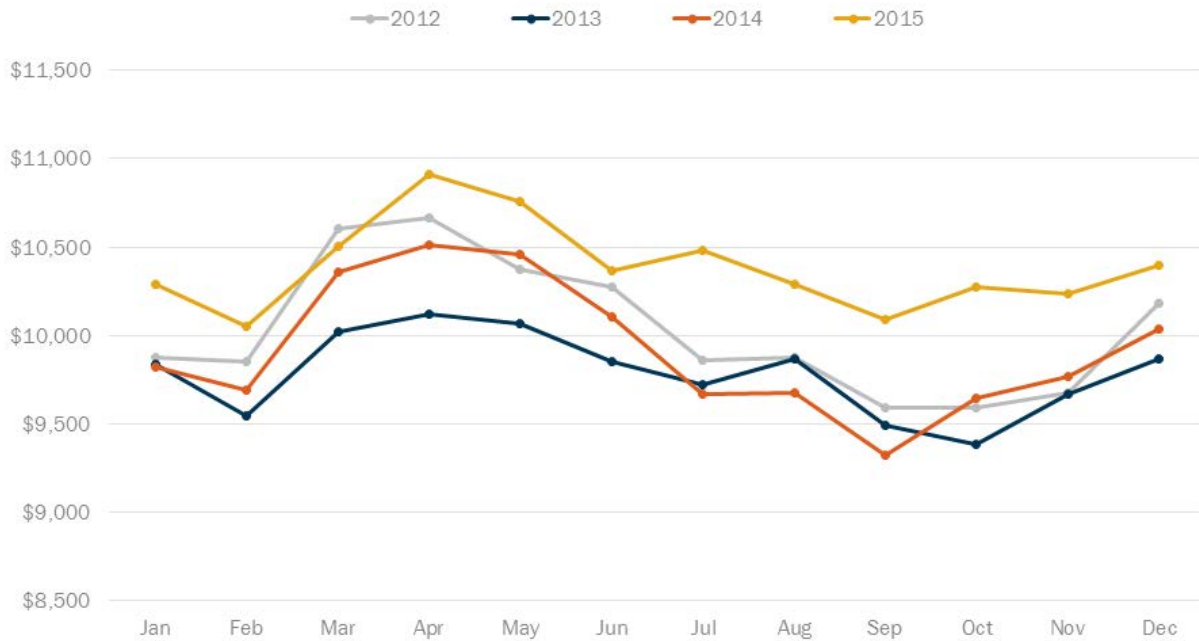
	2014 (Sept-Nov)	2015 (Sept-Nov)	Increase from 2014
CARS SOLD	8,047	9,779	22%

### WHOLESALE PRICES FOR DEALER-CONSIGNED UNITS JUMP IN 2015

Pricing for dealer-consigned units was strong all year, but especially in the second half. That was reflective of a retail market that also strengthened as the year

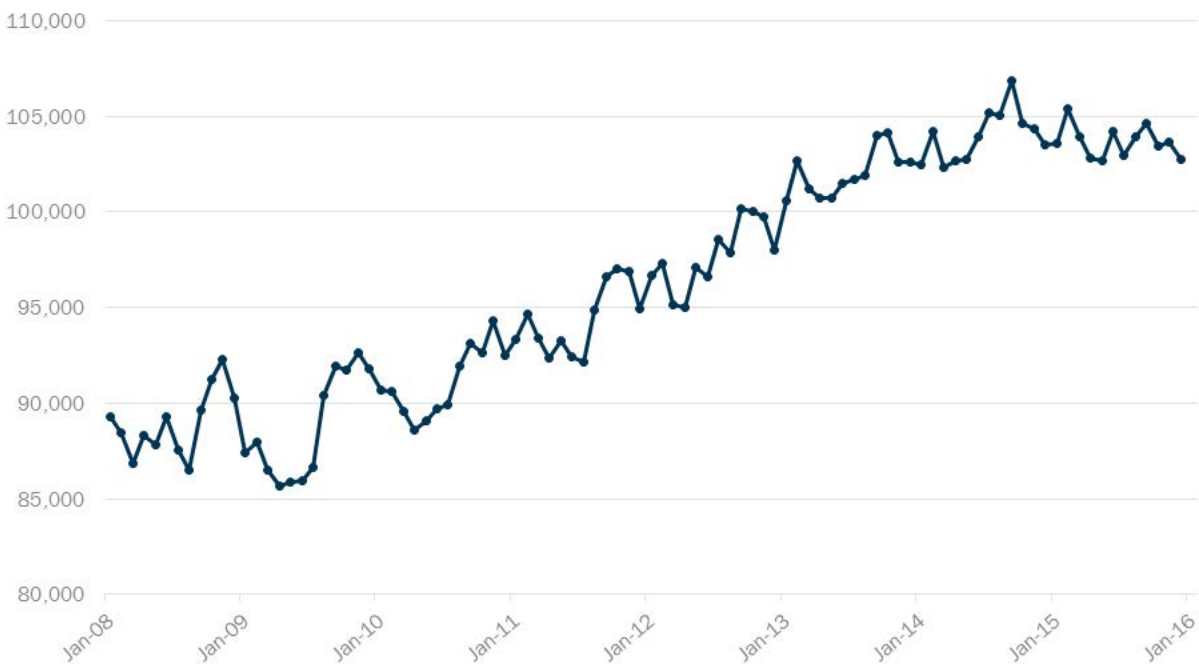
progressed. In addition, dealers were receiving newer trade-ins and better using the auction process for velocity management. After many years of moving upward, the average mileage on dealer-consigned units declined in 2015.

#### AVERAGE AUCTION PRICE—DEALER-CONSIGNED VEHICLES



Source: Manheim Consulting

#### AVERAGE MILEAGE—DEALER-CONSIGNED VEHICLES



Source: Manheim Consulting



**2016 USED CAR MARKET REPORT**

# **Q&A WITH 2016 NADA CHAIRMAN**

**JEFF CARLSON**

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NADA Chairman Jeff Carlson represents Colorado's dealers on the National Automobile Dealers Association board of directors. He is president of Glenwood Springs Ford and Glenwood Springs Subaru in Glenwood Springs, Colo., and is co-owner of Summit Ford in Silverthorne, Colo. NADA represents 16,500 new car and truck dealerships, with both domestic and international franchises.



**Q How would you describe business conditions for franchised dealers in 2015?**

**A** I would characterize it as a tale of two industries. The bright side is we may be experiencing the best sales period in history, exceeding the previous record of 17.4 million new vehicles. The dark side is the excessive regulatory pressures that seem to grow in depth and breadth from federal agencies. NADA has quantified regulatory compliance costs at a staggering \$183,000 per dealership.

**Q What do you see as the biggest challenge facing franchised dealers in 2016?**

**A** NADA's policy engagement efforts all have a common theme: protecting consumers from the unintended consequences of Washington's good intentions. Whether it's dealer-assisted financing, recalls, or other overreaching regulations, NADA has fought—and will continue to fight—to protect consumer rights, consumer choice, and consumer savings. Vehicle affordability must be a bedrock principle for national policy makers. Affordability expands consumer choice and drives consumer acceptance. Consumer acceptance drives fleet turnover. And fleet turnover results in economic growth, improved fuel efficiency, and safer vehicles on the roadways.

NADA will also continue to push back at the federal level against efforts that burden dealers with unnecessary or duplicative regulations, because they only generate duplicative compliance costs that are ultimately paid by consumers. Outside of the regulatory arena, one of my top priorities is ensuring that NADA continues to be a leader in helping our dealers meet the challenges of a changing industry, whether that's through innovative training offered at the NADA Academy, the work of the NADA 20 Groups, or efforts to get more NextGen dealers and managers involved with NADA.

**Q CPO sales continue to increase. How is this trend changing the way franchised dealers do business?**

**A** From an inventory standpoint, the increase in CPO sales is allowing dealers to look at more later-model year vehicles that our customers want. This ends up being beneficial to both dealers and used-vehicle shoppers.

**Q What tactics are franchised dealers using to increase customer satisfaction?**

**A** Customer satisfaction is the nature of the business, and dealers strive daily to exceed their customers' expectations. Consumers have the power of the Internet to gauge how customer-friendly a dealership is, and they use that extensively. The result is that dealers not only compete for customers based on price but also on the value of the total package from sales, service and customer friendliness. I recently saw a survey that asked car buyers to rate their sales experience as positive, neutral or negative. The responses were 90 percent positive, 6 percent neutral and 4 percent negative. To me, this validates the success the industry is having.

**Q What does increasing government regulation on vehicle financing, namely from the Consumer Financial Protection Bureau, mean for franchised dealers?**

**A** The attempted end-around the CFPB is using to change our business model is disruptive to dealers and to our financial services partners. More importantly, it's increasing the cost of credit for consumers, which makes it more difficult for dealers to sell and for consumers to buy. Dealers have the ability to beat the competition by discounting rates on auto loans.

**Q What changes are you seeing (or do you hope to see) in the acquisition and disposition of vehicles in the wholesale market?**

**A** Buying and selling vehicles has become easier with Internet auctions and the market has become more efficient. More dealers are participating. It has become easier to match product to the best market, and all of this is done in a matter of seconds today. The used-vehicle market is incredibly transparent today for both buyers and sellers.



**2016 USED CAR MARKET REPORT**

# **Q&A WITH 2016 NIADA PRESIDENT**

**FRANK FUZY**

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NIADA President Frank Fuzy is the owner of Century Motors of South Florida, one of the nation's largest online dealerships. Fuzy was the Florida Independent Auto Dealers Association's 2006 Florida Quality Dealer and was a nominee for the National Independent Auto Dealers Association's 2006 National Quality Dealer. He has previously served as president, secretary, treasurer and chairman of FIADA and as NIADA's treasurer, regional vice president and senior vice president.

**Q How would you describe business conditions for independent car dealers in 2015?**

**A** Business in 2015 was challenging, especially dealing with all the recalls that have been added to our plate as we work to do the right thing for our customers. It's a strange job now, and it takes time to shuffle cars to all the new car dealers for recall repairs. It's another free service we've added to our dealerships.

**Q What best practices are independent car dealers using to source inventory?**

**A** It's always a challenge to find the right car for the right price. Auctions are still the No. 1 source for independent dealers to find inventory—our latest member survey showed 88 percent are buying vehicles there—but the way they're buying at auction is changing as auctions add more services and online options continue to grow. More and more dealers are using technology to learn what vehicles are selling quickly in their market and for how much, so they can make sure they're buying the right vehicles to be more efficient and profitable.

**Q What is your advice to independent dealers looking to build their online business?**

**A** Online business is a must to survive in the future. I highly recommend a number of online vendors, including eBay Motors, Autotrader and Carfax Used Car Listings—all of which are NIADA Corporate Partners. Through eBay, our dealership is advertising worldwide, and with the ease of transportation and low shipping costs, we sell globally.

**Q Can you talk about the importance of NIADA Certified Pre-Owned vehicles to independent dealers?**

**A** The CPO program is a huge advantage for independent dealers. Now we, as used car dealers, can compete with the new car franchised dealers on a level playing field. The program includes a warranty on every car offered for sale that qualifies for certification. The good thing about using the NIADA Certified program is that you as the dealer pick the cars you want to certify, and if you pick the right cars, up-selling service contracts is an easy sell that will add profit to each sale and give the customer something of value. CPO units are very much in demand because the customers want the peace of mind that comes with the better vehicle and the warranty.

**Q What has your membership in NIADA meant for your business?**

**A** My No.1 goal as NIADA president is to increase membership. In numbers, we are powerful.

Think of the technology that's in cars now, and let's add all the laws, regulations and frivolous lawsuits today's dealer has to contend with. There is not enough time in a day to deal with all those issues. Being part of NIADA and the Florida IADA has made us what we are today. The association has helped us learn about all the products in the market that can help us be more efficient and profitable through its partner vendors. That's helped keep us on the cutting edge and ahead of the competition throughout our 31 years of success in the business.

We as dealers spend thousands of dollars on auto insurance for our dealership. The cost of membership in the state and national associations is a couple of hundred—a drop in the bucket. But just one bad law from D.C. or a restrictive regulation from your State House can affect your dealership or even put you out of business.

NIADA and the state associations invest those dues and spend countless hours working to keep that from happening. That alone is priceless. But there is also a financial payoff from the hundreds of member benefit programs available at the national and state levels.

**Q What changes are you seeing (or do you hope to see) in the acquisition and disposition of vehicles in the wholesale market?**

**A** With the price of new cars going up, luxury cars, used trucks and SUVs are bringing a premium. Online buying and selling is the wave of the future, and car dealers today need to be practicing that.

Just look at our founding fathers who started NIADA 70 years ago, and compare what they had to do to buy and sell a car then to just the disclosure statement on selling a car today. Dealing with all the state and federal agencies that regulate us today is the biggest issue we have to deal with.

Time is money, and there's not enough time in a day for a small independent dealer to handle all the issues out there now without a strong national and state association on his side, helping in every aspect to better his business.



## 2016 USED CAR MARKET REPORT

# Q&A WITH COX AUTOMOTIVE'S CHIEF CLIENT SUCCESS OFFICER

## RAJ SUNDARAM

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Raj Sundaram is Chief Client Success Officer at Cox Automotive, where he is responsible for helping clients increase efficiencies and grow their business utilizing the combined comprehensive solutions of the Cox Automotive brands. Sundaram had been with Dealertrack since 2006, where he had been co-president since November 2014. During his tenure at Dealertrack, which was acquired by Cox Automotive in 2015, Sundaram served in numerous roles, including executive vice president, group president and senior vice president of Dealer Solutions; and senior vice president of the Solutions and Services Group. Widely known as an automotive industry visionary, he has held management positions with Automotive Lease Guide (ALG) Inc.; Nissan North America; and Ford Motor Company, prior to Dealertrack.

**Q What technology trends are taking hold in the used car market that dealers should be aware of?**

**A** The biggest trends are how the car buying process has become more digital, from initial research and shopping all the way to acquisition and ownership. Dealers are using technology to create a stronger, more engaging customer experience around the car buying process before shoppers ever enter the dealership.

Today's shopper wants to do more and more online. By allowing the car shopper to start the process on the dealer's website, including searching for payment and finance options, submitting a credit application, and receiving a trade-in value online, dealers are creating more engagement opportunities through a digital platform than ever before. For example, Port City Nissan in Portsmouth, N.H., hit a new industry benchmark with a 49 percent Internet lead-to-sale close rate on finance leads by using Digital Retailing tools on its website.

**Q Many industry influencers and media are talking about the 60-minute car buying transaction. Will this become a reality in 2016?**

**A** Whether their goal is a 60-minute or 90-minute transaction, more retailers will need to make the shopping experience more compelling and convenient for car buyers. We think we'll see transaction times shrink in 2016 as dealers embrace technology to make the online to in-store transition more efficient and transparent. In addition, the overall experience will be more consistent with the goal of the customer—to get in and out of the physical dealership more quickly.

**Q What is the future of the F&I process in the used car market?**

**A** The future is bright. Thanks to technology, the F&I marketplace has evolved tremendously over the past 10 years or so. In surveys, consumers overwhelmingly are telling dealers they want to be able to self-select or self-educate on F&I options entering a dealership. This has been the No. 1 trend change in the F&I space in 2015, and we expect it to accelerate in 2016. The online education and selection of products either on a tablet in the dealership or the dealership's website is a familiar experience and consistent with what consumers do beyond buying a car. Shoppers may not know exactly what they want when it comes to F&I products, but they definitely want to find out more.

For the dealer, mobile tools, such as our Dealertrack eMenu for iPad, and the online presentation of F&I options through the use of tools like our MenuDriver, are helping lead to greater customer confidence in the sales process and additional F&I profits for the dealership. For example, based on our data from dealers using our eMenu for iPad, they are realizing a profit increase of \$281 per deal on F&I products, and a total revenue increase of \$18,528 per month.

**Q In your opinion, what has transformed the automotive retail space over the past year? And, what will help this space evolve even further in 2016?**

**A** Thanks to innovative technologies and progressive automotive retailers, the level of efficiency, empowerment, and transparency that has taken place in our industry over the past year has been astonishing. We expect this evolution and transformation of the car shopping experience to continue to take shape well into 2016 and beyond.

The implementation of technology into automotive retailing will undoubtedly ignite new revenue-generating opportunities for dealers as their customers become more engaged and loyal to their store and brand.

**Q How has the crackdown by state and federal regulators, such as the Federal Trade Commission (FTC), state attorneys general, and the Consumer Financial Protection Bureau (CFPB), affected the way we sell cars over the past couple of years and will in the future?**

**A** Over the past year, from disparate impact credit discrimination to deceptive advertising claims, dealers were in regulators' crosshairs. In the new year, we expect the agencies and the state AGs to increase their efforts in looking at how dealers sell aftermarket products just as they did with credit card issuers.

To protect your dealership from the next round of regulatory investigations on the aftermarket front, dealers should: research third-party service providers; review marketing and training materials; justify the value of the product in relation to cost; try to resolve customer complaints in-house before they go public; and take advantage of eMenu options to show consistency, transparency, and fairness in selling aftermarket products.

**Q How has digital advertising helped to better engage and retain car shoppers to deliver more qualified buyers into the showroom and drive bottom-line results?**

**A** Digital advertising is making the entire shopping and buying process more efficient for the customer, including the time spent in the dealership. Technology is making it possible for customers to control the pace and process more, and to make tangible progress toward their vehicle purchase before they decide to engage in person.

Digital advertising helps to build brand and dealership awareness at a local level by putting the right advertisement in front of the right consumer at the right time on the right website. We leverage our technology to locate car shoppers in their respective markets, and reach them in a progressive way that can escort them from a Tier 1 manufacturer's website down to a specific vehicle at a dealership in their neighborhood. It's a strategy that has been the foundation of our growth in this area, and has been the most effective tool that we've delivered to the dealers to help them optimize campaigns at a local level.

**Q How can dealers complement their vehicle sales through fixed operations?**

**A** Over the past 12 to 18 months, dealers have done an amazing job in the area of fixed operations. As automotive retailers extend technology into the service area to create more customer engagement opportunities, we believe this will set tremendous growth opportunities in motion. By simply leveraging tablet and digital technology in the service lane, we are seeing the customer service experience become more positive. These experiences are significant because they are paving the way with customers when it comes to moving them into their next vehicle in the years ahead.

**Q How are lending trends (prime and subprime) affecting the used car market?**

**A** During 2015, there were fears and concerns that the automotive lending market faced another subprime bubble like the one we saw back in 2008. In reality, based on our experience in the market, the credit picture is good for the American consumer, and we are in the best environment for automotive lending in years.

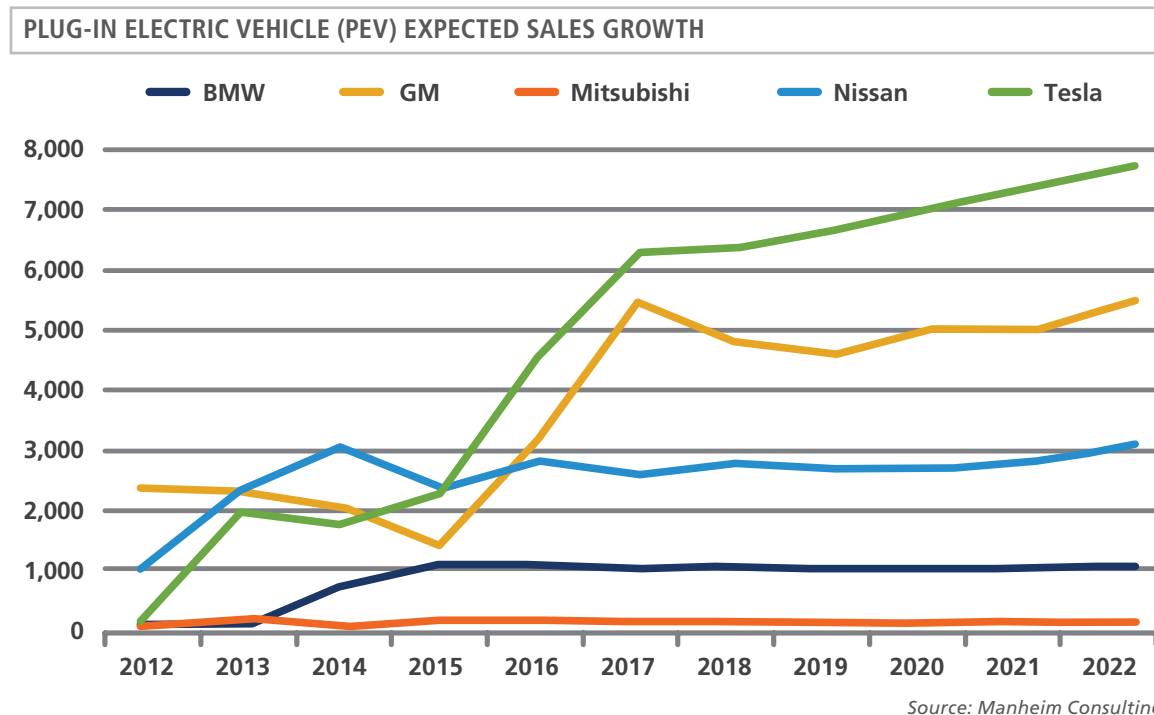
Used car demand has been very steady and is growing as the supply of used vehicles continues to rise. As this supply continues to recover, lenders are looking to help more and more consumers purchase vehicles. The opportunity for used car financing remains strong.

In 2014 and 2015, we saw growth in the number of full-spectrum lenders, or single lenders who offer a full range of prime and subprime financing options. We expect that roster of "one-stop" lenders to continue to grow through 2016.

## STRATEGY KEY TO SUCCESS IN GROWING ELECTRIC VEHICLE MARKET

By 2025, electric vehicles are expected to make up 25 percent of auto sales.

Dealers who understand trends in the electric vehicle market and create strong wholesale strategies now will be poised for success in the decades to come. Key factors to consider include tax incentives, geopolitical pressures, and population migration.



### Understand the Effect of Federal and State Tax Incentives

The American Clean Energy and Security Act of 2009 established tax credits for electric vehicles that can total \$7,500 depending on battery size. This federal incentive is available to all plug-in electric vehicles until each manufacturer has produced 200,000 qualifying vehicles across all models in the United States. At the state level, California, Washington, and Colorado have robust incentives in place that should shape remarketing strategies.

### Think Globally To Release Inventory Pressure: Geopolitics and Population Migration

Federal and state tax incentives are one of the main reasons lease penetration for PEVs is much higher than for traditional cars (75 percent vs. 28 percent), which in turn has created an inventory management challenge for OEMs and their captive finance partners.

With such a high number of lease returns for electric vehicles creating a glut of inventory in the market, consignors must think globally when considering ways to release inventory pressure. The U.S. is not the only country that has incentivized the growth of the electric vehicle market, and there are pockets of demand placed around the world.



Population migration is another large driver for electric vehicle adoption. By 2025, there are expected to be 40 regions with a population of over 10 million around the world. This effect of cities becoming denser will drive the adoption of cleaner vehicles as well as car sharing, both of which will benefit electric vehicle sales.

As the global electrified vehicle market looks to grow to 30 million new units produced in 2025, a greater emphasis will be placed on adequately and strategically remarketing these units. This will require separate domestic and global strategies for PEVs. Being able to quickly capitalize on changing factors in the U.S. and abroad will determine whether a consignor is successful or not with its PEV remarketing strategy. ■

## THE KEY TO GETTING TOP DOLLAR AT AUCTION? RECONDITIONING

Dealers who participated in a panel at the 2015 CAR conference unanimously agreed that they were willing to pay more for a reconditioned unit.

This was not a surprising position. Reconditioned units save time and money for dealers. A reconditioned vehicle incurs lower detailing costs and is front-line-ready quickly, which is critical to a dealer's bottom line.

In order to help sellers make informed decisions about reconditioning and ensure return on investment, Manheim examined all commercial sales made in the U.S. during 2014 (excluding TRA/Salvage, Specialty, and pre-recon grades of less than 2.5) to learn how a vehicle's initial grade and value impact retention. The accompanying charts demonstrate the impact of paint and body spending on grade improvement.

### Key findings include:

- The best candidate for reconditioning is a lower-grade, higher-value vehicle.
- Higher ROI is realized on improving lower grade units; higher incremental MMR percent increases are observed for lower grade units.
- Reconditioning higher-value vehicles naturally has a higher ROI; a 1 percent MMR lift on a \$20,000 vehicle equates to \$200, versus \$100 for a \$10,000 vehicle.
- Depending on the initial grade and vehicle value, achieving an ROI of greater than \$1 may require moving grade by more than 0.1 or 0.2 points.
- Careful selection of reconditioning services to increase grade for the lowest spend is critical.

### AVERAGE PAINT AND BODY SPEND AND GRADE IMPROVEMENT

AVERAGE VALUE: \$10,000

	Grade Improvement →									
	\$110 0.1	\$161 0.2	\$206 0.3	\$254 0.4	\$304 0.5	\$362 0.6	\$413 0.7	\$450 0.8	\$483 0.9	\$431 1.0
2.5	\$0.74	\$0.98	\$1.12	\$1.19	\$1.21	\$1.19	\$1.19	\$1.21	\$1.23	\$1.49
2.6	\$0.70	\$0.94	\$1.07	\$1.13	\$1.15	\$1.13	\$1.12	\$1.14	\$1.17	\$1.41
2.7	\$0.67	\$0.89	\$1.02	\$1.07	\$1.09	\$1.07	\$1.06	\$1.08	\$1.10	\$1.33
2.8	\$0.64	\$0.85	\$0.96	\$1.01	\$1.03	\$1.01	\$1.00	\$1.02	\$1.03	\$1.24
2.9	\$0.60	\$0.80	\$0.91	\$0.96	\$0.97	\$0.95	\$0.94	\$0.95	\$0.96	\$1.16
3.0	\$0.57	\$0.75	\$0.86	\$0.90	\$0.91	\$0.89	\$0.88	\$0.89	\$0.90	\$1.07
3.1	\$0.54	\$0.71	\$0.81	\$0.84	\$0.85	\$0.83	\$0.82	\$0.82	\$0.83	\$0.99
3.2	\$0.50	\$0.66	\$0.75	\$0.79	\$0.79	\$0.77	\$0.75	\$0.76	\$0.76	\$0.90
3.3	\$0.47	\$0.62	\$0.70	\$0.73	\$0.73	\$0.71	\$0.69	\$0.69	\$0.69	\$0.82
3.4	\$0.44	\$0.57	\$0.65	\$0.67	\$0.67	\$0.65	\$0.63	\$0.63	\$0.63	\$0.74
3.5	\$0.41	\$0.53	\$0.59	\$0.61	\$0.61	\$0.59	\$0.57	\$0.56	\$0.56	\$0.65
3.6	\$0.37	\$0.48	\$0.54	\$0.56	\$0.55	\$0.53	\$0.51	\$0.50	\$0.49	\$0.57
3.7	\$0.34	\$0.44	\$0.49	\$0.50	\$0.49	\$0.47	\$0.45	\$0.43	\$0.42	\$0.48
3.8	\$0.31	\$0.39	\$0.44	\$0.44	\$0.43	\$0.41	\$0.38	\$0.37	\$0.35	\$0.40
3.9	\$0.27	\$0.35	\$0.38	\$0.38	\$0.37	\$0.34	\$0.32	\$0.31	\$0.29	\$0.31
4.0	\$0.24	\$0.30	\$0.33	\$0.33	\$0.31	\$0.28	\$0.26	\$0.24	\$0.22	\$0.23
4.1	\$0.21	\$0.26	\$0.28	\$0.27	\$0.25	\$0.22	\$0.20	\$0.18	\$0.15	
4.2	\$0.17	\$0.21	\$0.22	\$0.21	\$0.19	\$0.16	\$0.14	\$0.11		
4.3	\$0.14	\$0.17	\$0.17	\$0.16	\$0.13	\$0.10	\$0.08			
4.4	\$0.11	\$0.12	\$0.12	\$0.10	\$0.07	\$0.04				
4.5	\$0.07	\$0.08	\$0.06	\$0.04	\$0.01					
4.6	\$0.04	\$0.03	\$0.01	-\$0.02						
4.7	\$0.01	-\$0.01	-\$0.04							
4.8	-\$0.03	-\$0.06								
4.9	-\$0.06									

Source: Manheim Consulting

By carefully evaluating their reconditioning strategy, sellers can increase retention at auction. While reconditioning should be completed on lower-grade and higher-value units, spending additional time to evaluate recon potential on all units can greatly improve ROI. Sellers should first consider the combination of pre-recon grade and vehicle value. The ideal candidate for reconditioning is a lower-grade, high-value unit. If the vehicle falls into a questionable category, the seller must determine whether items can be repaired for less than the breakeven costs, so the investment will pay for itself. The cost to repair damages does not move linearly with the grade. Multiple items may be repaired for under the breakeven cost, thereby moving the grade enough that the MMR percentage lift is higher than the reconditioning spend. ■

**AVERAGE PAINT AND BODY SPEND AND GRADE IMPROVEMENT**

AVERAGE VALUE: \$20,000

	Grade Improvement →									
	\$110	\$161	\$206	\$254	\$304	\$362	\$413	\$450	\$483	\$431
	0.1	0.2	0.3	0.4	0.5	0.6	0.7	0.8	0.9	1.0
2.5	\$1.47	\$1.96	\$2.25	\$2.37	\$2.42	\$2.38	\$2.37	\$2.42	\$2.47	\$2.99
2.6	\$1.41	\$1.87	\$2.14	\$2.26	\$2.30	\$2.26	\$2.25	\$2.29	\$2.33	\$2.82
2.7	\$1.34	\$1.78	\$2.03	\$2.14	\$2.18	\$2.14	\$2.12	\$2.16	\$2.20	\$2.65
2.8	\$1.27	\$1.69	\$1.93	\$2.03	\$2.06	\$2.02	\$2.00	\$2.03	\$2.06	\$2.48
2.9	\$1.21	\$1.60	\$1.82	\$1.91	\$1.94	\$1.90	\$1.88	\$1.90	\$1.93	\$2.31
3.0	\$1.14	\$1.51	\$1.72	\$1.80	\$1.82	\$1.77	\$1.75	\$1.77	\$1.79	\$2.15
3.1	\$1.08	\$1.42	\$1.61	\$1.68	\$1.70	\$1.65	\$1.63	\$1.64	\$1.66	\$1.98
3.2	\$1.01	\$1.33	\$1.51	\$1.57	\$1.58	\$1.53	\$1.51	\$1.51	\$1.52	\$1.81
3.3	\$0.94	\$1.24	\$1.40	\$1.46	\$1.46	\$1.41	\$1.38	\$1.39	\$1.39	\$1.64
3.4	\$0.88	\$1.15	\$1.29	\$1.34	\$1.34	\$1.29	\$1.26	\$1.26	\$1.25	\$1.47
3.5	\$0.81	\$1.06	\$1.19	\$1.23	\$1.22	\$1.17	\$1.14	\$1.13	\$1.11	\$1.30
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3.8	\$0.61	\$0.79	\$0.87	\$0.88	\$0.86	\$0.81	\$0.77	\$0.74	\$0.71	\$0.80
3.9	\$0.55	\$0.70	\$0.76	\$0.77	\$0.75	\$0.69	\$0.64	\$0.61	\$0.57	\$0.63
4.0	\$0.48	\$0.61	\$0.66	\$0.65	\$0.63	\$0.57	\$0.52	\$0.48	\$0.44	\$0.46
4.1	\$0.41	\$0.52	\$0.55	\$0.54	\$0.51	\$0.45	\$0.40	\$0.35	\$0.30	
4.2	\$0.35	\$0.43	\$0.45	\$0.43	\$0.39	\$0.33	\$0.27	\$0.22		
4.3	\$0.28	\$0.34	\$0.34	\$0.31	\$0.27	\$0.21	\$0.15			
4.4	\$0.21	\$0.25	\$0.24	\$0.20	\$0.15	\$0.09				
4.5	\$0.15	\$0.16	\$0.13	\$0.08	\$0.03					
4.6	\$0.08	\$0.07	\$0.02	-\$0.03						
4.7	\$0.01	-\$0.02	-\$0.08							
4.8	-\$0.05	-\$0.12								
4.9	-\$0.12									

Source: Manheim Consulting

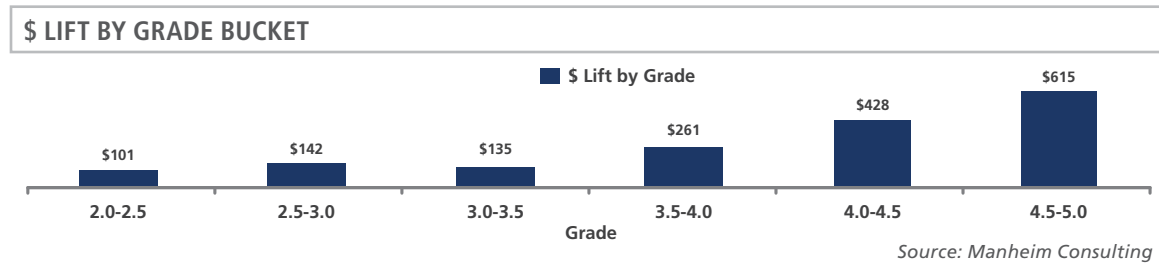
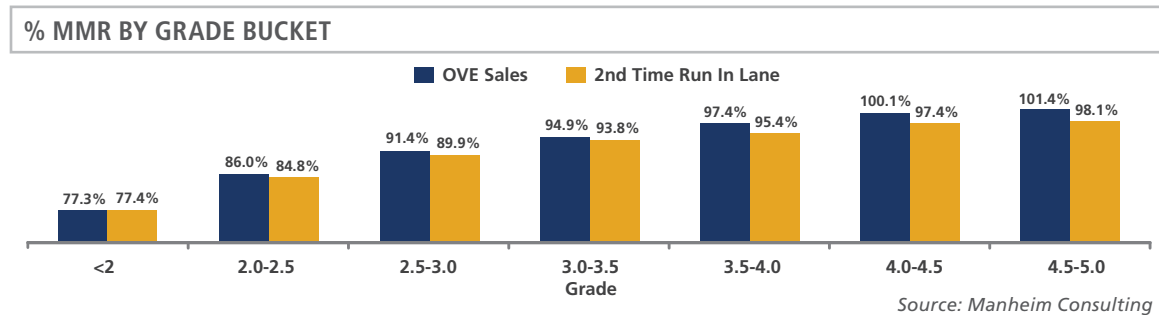
## FROM NO-SALE TO ONLINE SALE

Dealers whose vehicles don't sell the first time down the auction lane are increasing profits by listing unsold units on OVE.com rather than waiting for the next auction day.

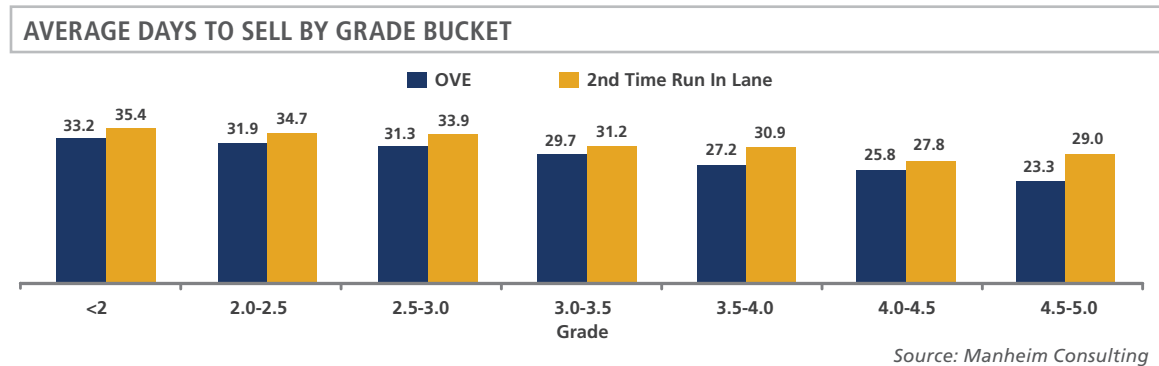
Only 55 percent of vehicles that run through the auction lane will sell the first time. Vehicles that do not sell the first time around, commonly referred to as "no-sales," are parked until the next week's sale or listed on OVE.

In an analysis of 15 national commercial customers that list all their "no-sales" on OVE, the vehicles sold on the site outperformed the vehicles run a second time in the physical auction lane in both MMR percentage and time to sell.

The lift in price attained from selling a "no-sale" on OVE ranges from \$144 for grade 2 vehicles to \$396 for the highest grades.



In terms of time to sell, listing no-sales on OVE immediately rather than waiting a week to re-run in-lane decreased days to sell by 3.9. With the cost of money at a 3.25 percent prime interest rate, the \$1.07 per car per day interest paired with the standard depreciation rate of 1.5 percent a month makes the carrying cost per car per day \$7.07. A reduction of 3.9 days brings the per car impact to \$27.57, which could add up to a \$27,570 savings on a no-sale portfolio of 1,000 units per year. ■



This is a summary. To view more information, visit: [www.manheim.com/content\\_pdfs/products/Increase-Auction-Values-Listing-No-Sales.pdf](http://www.manheim.com/content_pdfs/products/Increase-Auction-Values-Listing-No-Sales.pdf)

2016 USED CAR MARKET REPORT

# RENTAL

## 2015 HIGHLIGHTS

Total rental car industry revenue reached a record \$27.1 billion in 2015, a 4 percent increase from 2014.

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As in recent years, the biggest increases in 2015 came in off-airport, leisure and insurance replacement demand.

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Total rental revenue per unit was weak in 2015. The downward adjustment in rental fleet size, however, should allow for better revenue-per-vehicle numbers in 2016.

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The number of vehicles purchased by rental companies increased 9 percent to 1.78 million in 2015, the highest purchase volume since 2007.

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Relative to total new vehicle sales, rental's share was just over 10 percent in 2015. In 2005 and 2006, rental's share was more than 12 percent, so clearly manufacturers are not pushing units into rental service, which should have a positive impact on residuals.

**RENTAL INDUSTRY REVENUE INCREASES IN 2015**

Total rental car industry revenue reached a record \$27.1 billion in 2015. This represented a 4 percent increase from 2014, and it brought total revenue 35 percent higher than during the cyclical trough in 2009. As in recent years, the biggest increases in 2015 came in off-airport, leisure and insurance replacement demand. On-airport commercial revenue was weak, especially in light of ongoing increases in business air travel.

Also, as has been the case in recent years, total rental revenue per unit was weak in 2015. The downward adjustment in the rental fleet size that occurred in 2015 should, however, allow for better revenue-per-vehicle numbers in 2016.

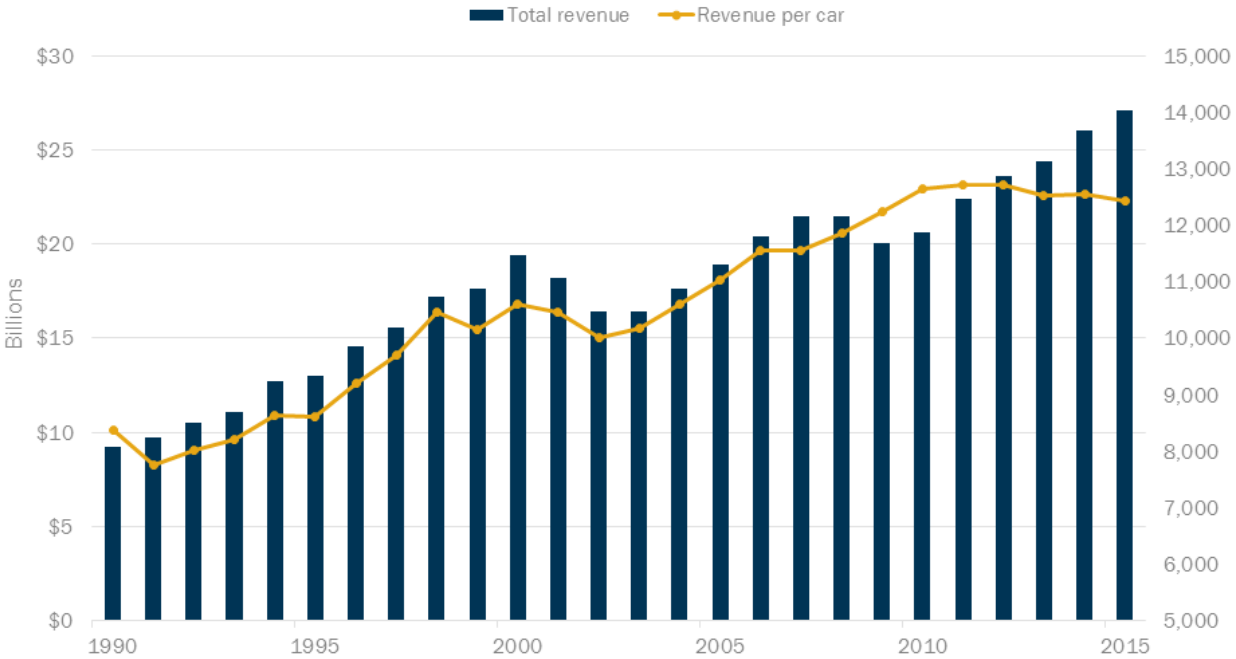
Despite three companies owning more than 95 percent of the rental fleet, the industry has always been characterized by intense price competition. In fact, pricing power, as measured by revenue per day, has

greatly lagged the sorts of increases that hotels and airlines have been able to achieve in revenue per room and revenue per seat mile during the past several years. If, as expected, vehicle depreciation costs rise in coming years, the industry will need stronger revenue-per-day performance. It will also need to boost that number to offset higher interest rates. The money factor is important to rental companies, as the operators of large fleets, whether they are funding through the ABS market, self-funding or leasing a portion of their fleet.

Although history suggests there is a positive correlation between fleet costs and rental rates, the traditional rental revenue stream is not immune to some skimming-off by new entrants. In the past, the lack of pricing power was simply explained away as commodity-like pricing in a competitive industry dominated by the most cost-effective producer; but today we have to consider that the industry is slowly being redefined beyond daily rental to include ride-sharing and car-sharing.

Manheim data indicate that in the third quarter of last year, rental car companies remarketed vehicles with 3,756 different year, make, model and body configurations. In the third quarter of 2015, it took 85 unique year, make, model and body configurations to account for 50 percent on all rental risk sales at auction. As recently as the third quarter of 2011, it took only 31 such unique configurations.

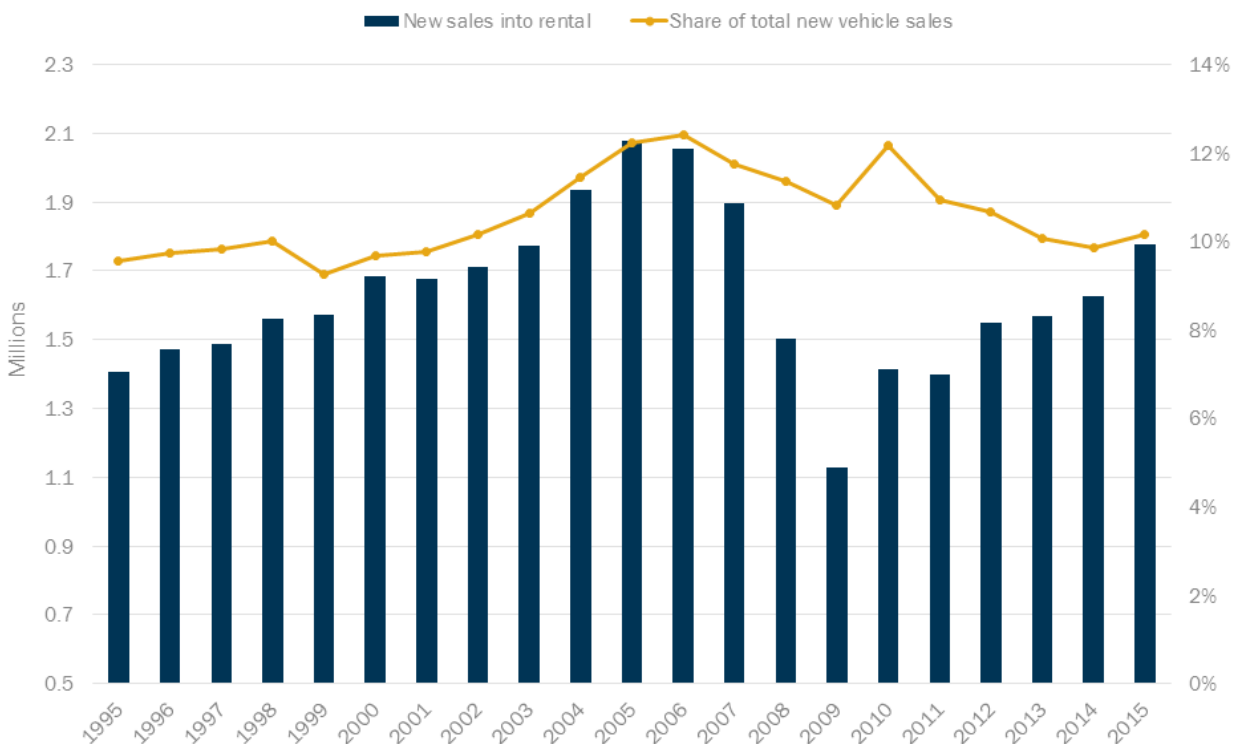
**U.S. CAR RENTAL MARKET REVENUE**



Source: Auto Rental News



## NEW VEHICLE SALES INTO RENTAL



Source: Auto Rental News & Automotive News

Auto manufacturers and rental car companies have invested in, or developed, car-sharing services while ride-sharing apps, such as Uber and Lyft, after already disrupting the taxi industry, may now alter when and how consumers decide to rent cars.

### NEW VEHICLE SALES INTO RENTAL REACH 1.78 MILLION IN 2015

The number of vehicles purchased by rental companies increased 9 percent to 1.78 million in 2015. It was the highest purchase volume since 2007, but well below the 2.1 million new vehicles that were sold into rental in 2005 and 2006. Given the shift from program to risk units (and a longer average service life for risk vehicles), rental company purchases of new vehicles are not expected to reach 2 million units a year any time soon. Relative to total new vehicle sales, rental's share was just over 10 percent in 2015, and consistent with 2014's share. In both 2005 and 2006, rental's share of new vehicle sales was more than 12 percent. Clearly, manufacturers are not pushing units into rental service, and that should have a positive impact on residuals.

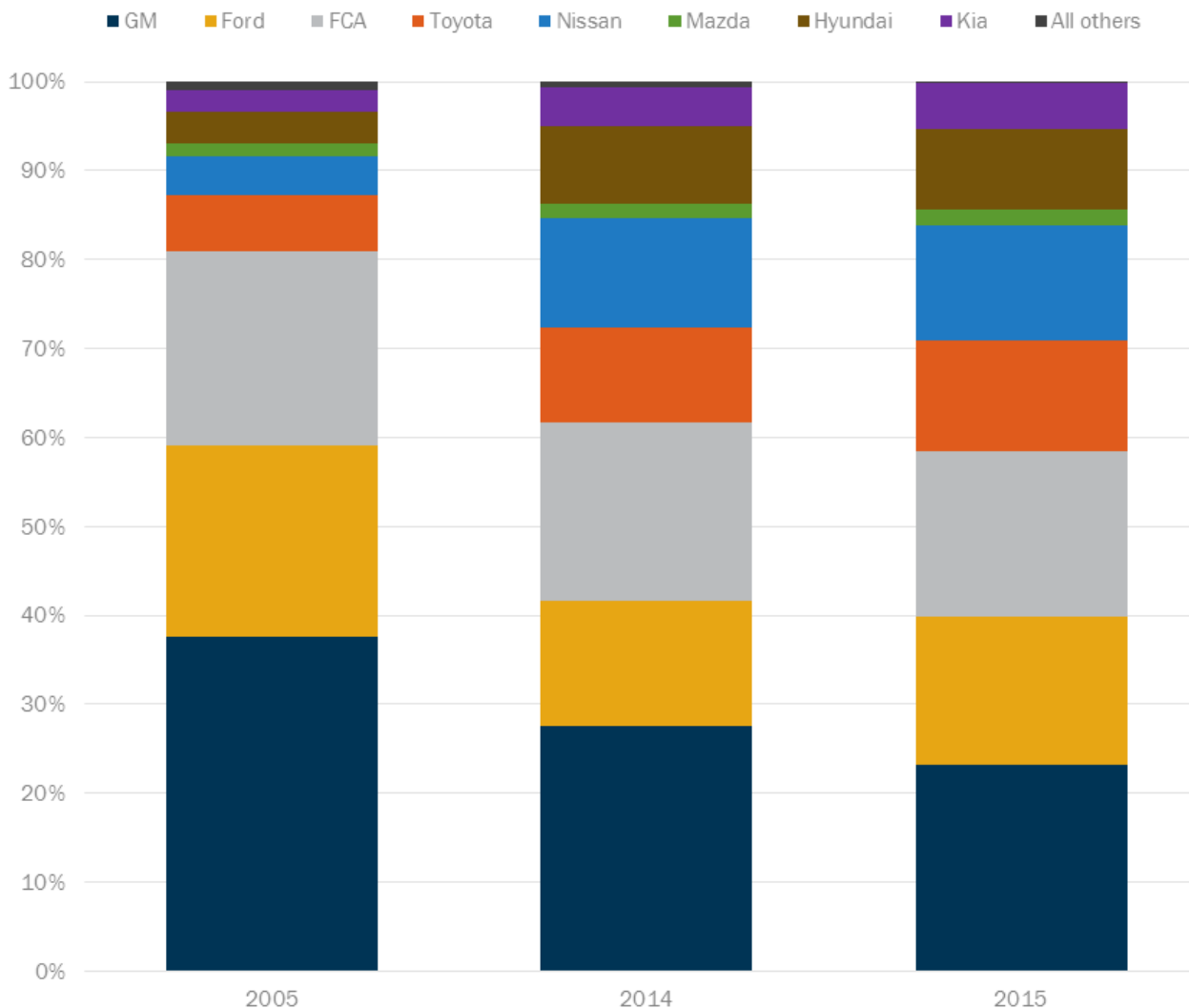
New vehicle sales into rental in 2015 were front-loaded into the first half of the year, with sales through June accounting for 58 percent of full-year purchases. Much of this was a result of a significant refreshing of the fleet at Hertz. This also meant that the remarketing of off-rental units was also much stronger in the first half of the year than in the second half.

The shifting pattern of purchasing, rental demand, and remarketing enticed some rental car companies to buy more used vehicles at auction to supplement their fleet. And, of course, with all of the majors now involved in all segments of the business, there is a greater opportunity to cascade vehicles down from premium brands to value brands as the units age.

The share of new vehicles sold into rental accounted for by domestic manufacturers fell for the fifth consecutive year in 2015. It marked their lowest share ever—even lower than 2009, when the GM and Chrysler bankruptcies forced rental companies to shift their purchasing patterns. Although both Ford and Chrysler posted double-digit increases in new vehicle sales into rental, it was from a low base and was mostly offset by declining rental sales for GM. Toyota, Hyundai and Kia all posted significantly higher sales into rental for the year.

Generally speaking, over the past decade, the mix of manufacturers and models making up the rental fleet—as well as the option contenting of the vehicles—has become more representative of overall retail new vehicle sales. For individual rental car companies, the shift toward a more diverse fleet has been even more striking since, in earlier times, some of the companies had major supply agreements with only one or two manufacturers. The greater mix of models in the off-rental supply has had several implications for remarketing—most of them positive. Most important,

DISTRIBUTION OF NEW VEHICLE SALES INTO RENTAL BY MANUFACTURER



Source: Bobit Business Media

it has helped protect residual values since one rental company is no longer forced to sell large numbers of any one model at any one time. It also means that the rental car company is not as susceptible to the negative consequences of an individual model having weak residual performance or being subject to a recall. The wider mix of off-rental units has, however, required that rental companies (and their auction partners) work harder to ensure specific vehicles get exposed to the dealers most interested in that particular product.

Manheim data indicate that in the third quarter of last year, rental car companies remarketed vehicles with 3,756 different year, make, model and body configurations. In the third quarter of 2015, it took 85 unique year, make, model and body configurations to account for 50 percent on all rental risk sales at auction. As recently as the third quarter of 2011, it took only 31 such unique configurations.

**RENTAL FLEET SIZE REMAINS STABLE IN 2015**

The total number of vehicles operating in rental fleets grew 5 percent in 2015, to 2.2 million units, according to *Auto Rental News*. Hertz went through a major refresh and rationalization of its fleet in 2015, and as a result, its fleet size had declined by year-end. Both Enterprise and Avis/Budget showed an increase in fleet size.

Hertz reported that 70 percent of its fleet purchases were accounted for by risk units in 2015, down from 79 percent in 2014. At 50 percent, Avis/Budget has the smallest share of its fleet purchases composed of risk units, and that percentage was down from 58 percent in 2014, but up from only 1 percent a decade ago. Purchases at Enterprise and the small independent rental car companies are almost exclusively risk units. Rental car companies have recently commented that pricing for program units in 2016 is not as favorable as 2015; thus, they anticipate a shift back to purchasing more risk units.

RENTAL RISK VEHICLES REMARKETED AT AUCTIONS

	3 <sup>RD</sup> QTR 2011	3 <sup>RD</sup> QTR 2014	3 <sup>RD</sup> QTR 2015
Number of unique year, make, model, body (YMMB) configurations sold	2,216	3,303	3,756
Share accounted for top 10 YMMB	28.2%	17.3%	15.6%
Share accounted for top 25 YMMB	46.5%	21.7%	26.9%
Number of YMMB to reach 50% share	31	86	85

Source: Manheim Consulting

**RENTAL RISK PRICING AT AUCTION REMAINS IN A NARROW RANGE**

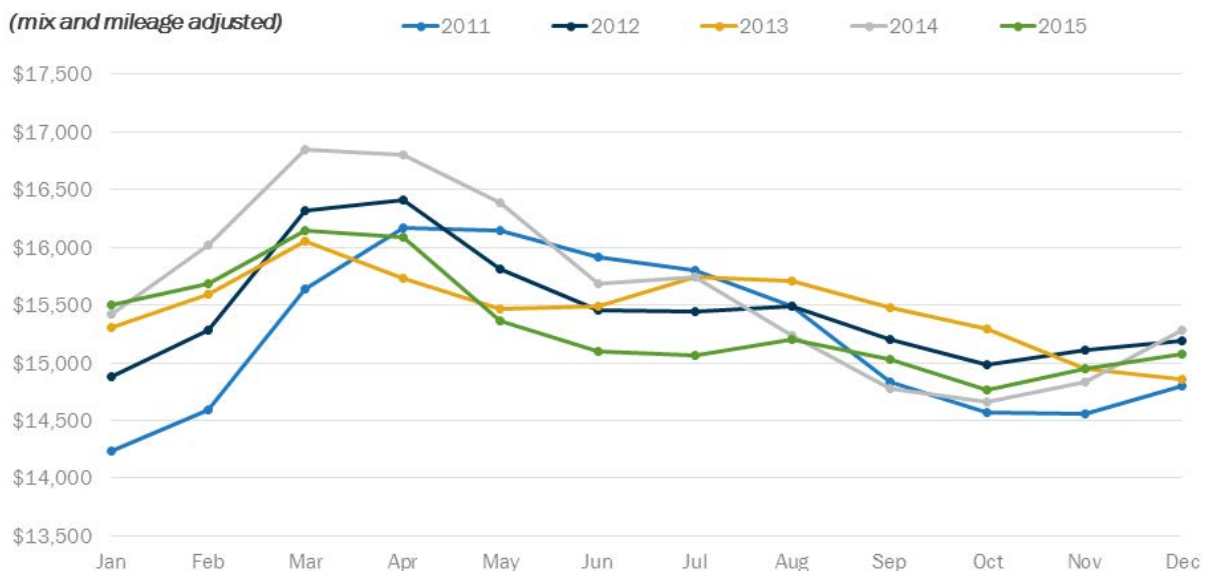
In 2015, prices for rental risk units sold at auction were similar to what was experienced over the past four years. Our index of mix- and mileage-adjusted prices for rental risk units did underperform in the summer months, but that was the result of Hertz’s selling rougher condition vehicles as it significantly refreshed its fleet. In the second quarter of 2015, only 30 percent of the rental risk units sold at auction had a condition grade of 4.0 or higher; whereas in the year-ago quarter, above average vehicles accounted for 45 percent of all sales.

Although our index of rental risk prices at auction appears to have significantly outperformed the overall

wholesale market, we would caution against such simple comparisons. Yes, auction prices for end-of-service rental units have been strong; but those vehicles represent a unique slice of the overall wholesale market. It is a segment that is susceptible to swings in new vehicle inventory levels and pricing—both of which have been favorable of late.

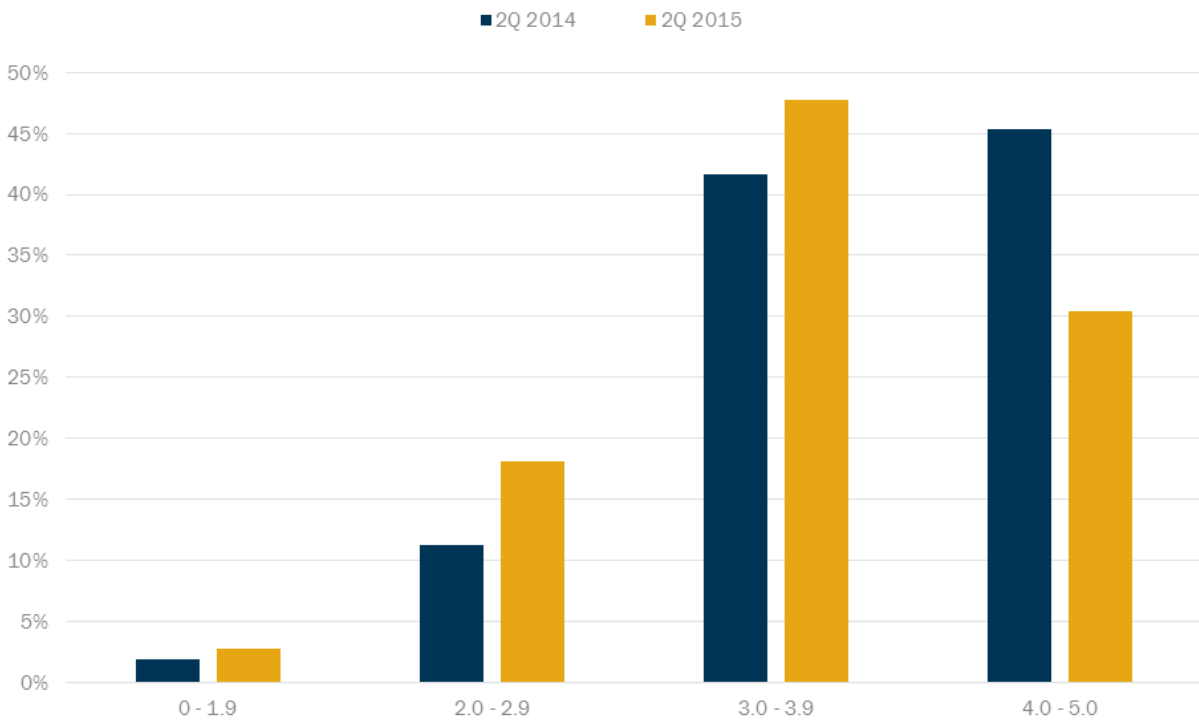
For example, the Bureau of Economic Analysis (as part of national income accounting) produces a monthly series of average prices for new vehicles bought by businesses. If we take that series and relate it to the mix- and mileage-adjusted price series for rental risk units produced by Manheim, we find that off-rental auction prices are indeed performing well; but the results are not outside of historic norms.

AVERAGE AUCTION PRICE—RENTAL RISK UNITS



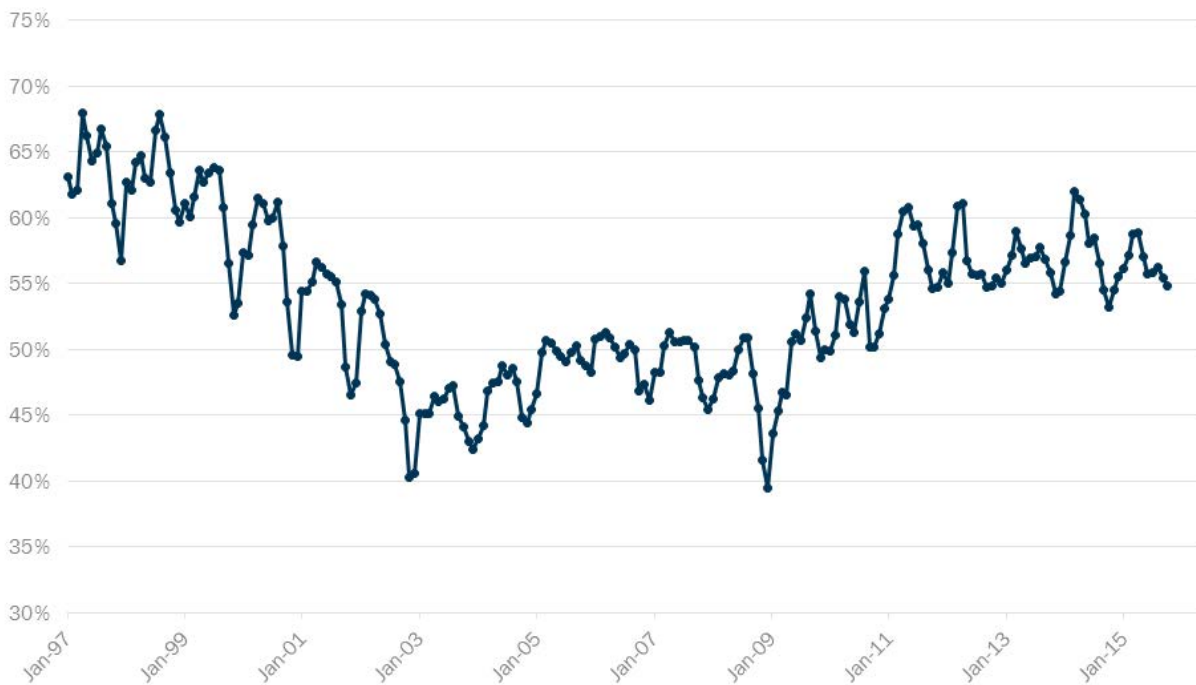
Source: Manheim Consulting

RENTAL RISK UNITS SOLD—DISTRIBUTION BY CONDITION



Source: Manheim Consulting

RENTAL RISK AUCTION PRICE VS. NEW VEHICLE SALE PRICE (BUSINESS) ONE YEAR PRIOR

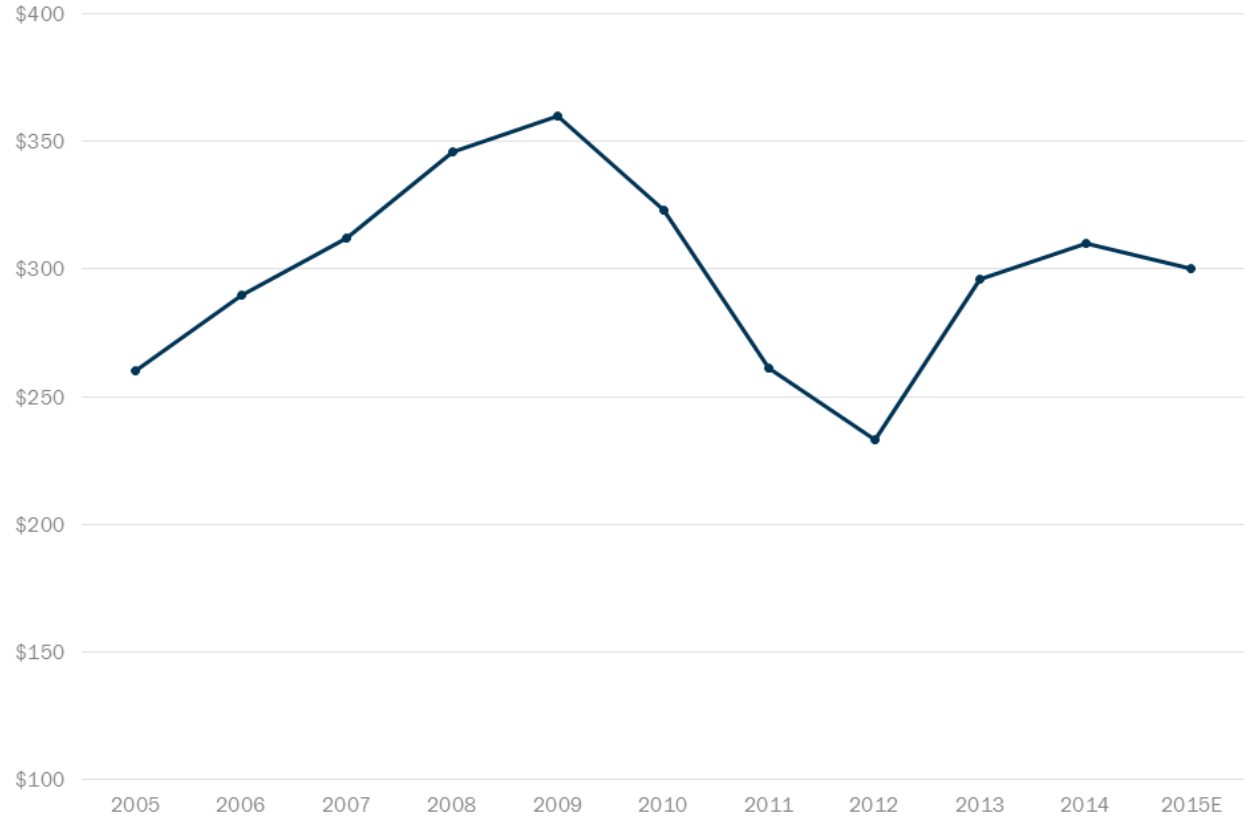


Source: BEA & Manheim Consulting

There is some justifiable concern that the influx of off-lease units in 2016 and beyond may dampen pricing for off-rental units. Although these two wholesale segments are not exactly great substitutes for each other (the distribution of model years, makes, and contenting is very different), there is the issue of share of the dealer’s mind and wallet. In coming years, returning lessees will be driving high-quality inventory right to the dealer’s door, and lessors will be enticing grounding dealers (with carrots and sticks) to buy these units at fair market value (or sometimes even less) with no buy fee. Each such acquisition will mean that dealer has need for one less unit from other sources.

However, the biggest influence on off-rental pricing will, as always, be manufacturer practices with respect to incentives and inventory levels. On that front, manufacturers, of late, have been better at equating production with demand. But the real test will come in future years when the pace of new vehicle sales levels off. Most rental car companies are expecting—and planning for—a higher per-vehicle monthly depreciation cost in 2016, but nothing like 2008 and 2009.

AVERAGE MONTHLY PER-UNIT FLEET COSTS FOR AVIS BUDGET GROUP



Source: Avis Budget Group

Digital remarketing of off-rental units is also driven by the fact that fleets are often concentrated in a particular geography—so much so that they can swamp local demand. Digital remarketing allows the seller to efficiently bring the buyer to the car rather than guess where to move the car.

**PRIOR RENTAL USE DOES NOT DIMINISH RESIDUAL VALUE**

As part of court cases in states where dealers are required to disclose a vehicle’s prior use as a rental to the retail buyer, we were asked to conduct an analysis of whether there is any diminution in value for a vehicle that was previously used as a rental, as opposed to one which was not. On a multiyear, annual and monthly basis, we looked at all individual year, make and body configurations for which there was an adequate sample size of both rental and nonrental sales at auction. After controlling for mileage, vehicle condition and seasonality, a regression analysis showed that in many cases, the results were statistically insignificant and in all cases small in magnitude—sometimes positive for the rental units and sometimes negative. Now, it is true that if a manufacturer sells a large number of a particular model into rental, it can harm the residual value of that model; but it does so for both the units owned by rental fleets and those owned by retail customers.

**RENTAL CAR COMPANIES GROW DIGITAL REMARKETING**

Rental car companies have been quick to adopt, as well as develop, innovative technologies and strategies to remarket end-of-service units. The reason is simple—fleet depreciation is a major determinant of

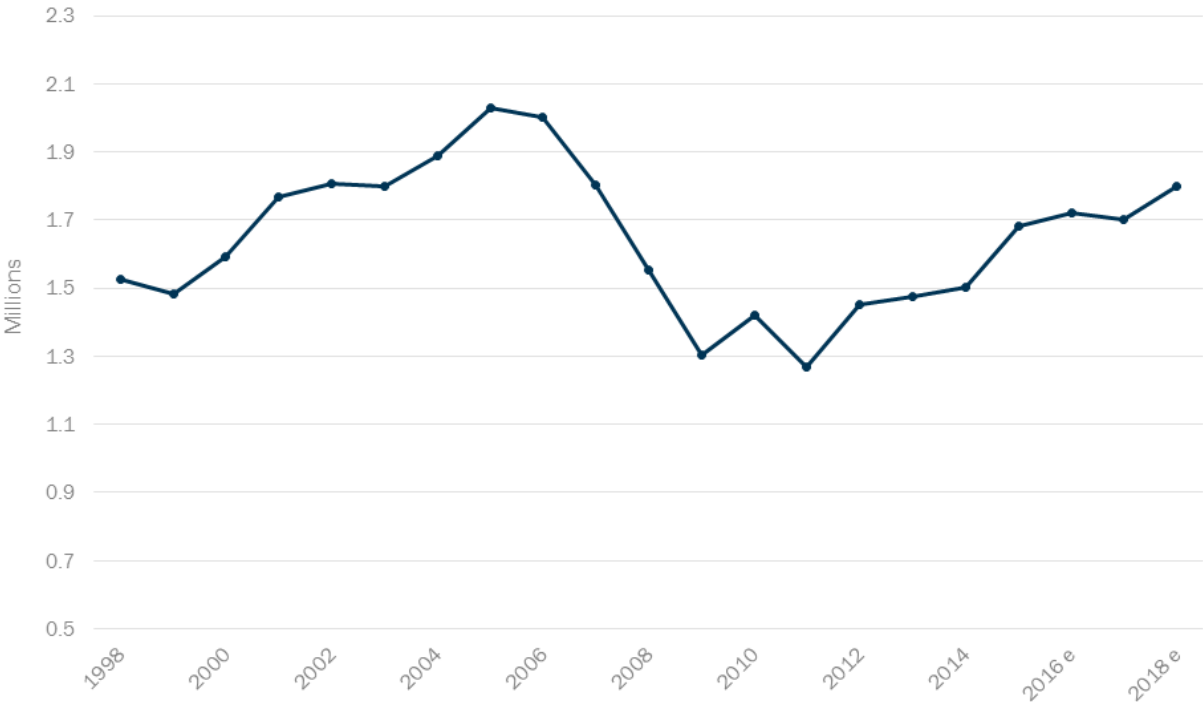
company profitability. When it comes to upstream remarketing, the rental companies have advantages and disadvantages. On the plus side, rental companies are long-established sellers in the wholesale market (which builds buyer trust), their end-of-service fleet is large, it is concentrated in a relatively narrow mileage and price range, and it often needs only modest reconditioning.

The disadvantage that rental companies face in selling upstream is that their time pressures are acute, and they certainly don’t want to marshal unproductive units. As such, the companies have developed strategies to pre-offer units while they are still in service as rental units.

Digital remarketing of off-rental units is also driven by the fact that fleets are often concentrated in a particular geography—so much so that they can swamp local demand. Digital remarketing allows the seller to efficiently bring the buyer to the car rather than guess where to move the car.

Another remarketing technique that some rental car companies have used successfully is the offering of specific makes in conjunction with the factory sale of that brand on auction day. To be successful at that, rental car companies need to ensure that their offerings blend better with the other units in the lane. In other words, they need to do more reconditioning and strive for a consistently higher conversion rate.

**TOTAL WHOLESALE SUPPLY: OFF-RENTAL**



Source: Manheim Consulting

## REMARKETING VOLUMES CONTINUE TO GROW

In 2015, approximately 1.66 million off-rental vehicles entered the wholesale market. Of these, some 780,000 units were sold at NAAA-member auctions. Another 200,000-plus were sold directly to retail customers, and the remainder were sold directly to dealers outside the traditional auction process. In 2016, off-rental volumes are expected to grow to close to 1.8 million and remain in that range in the years beyond. The future growth in off-rental volumes should mirror the growth in the total rental fleet size, as we foresee no significant change in holding periods.



2016 USED CAR MARKET REPORT

# LEASING

## 2015 HIGHLIGHTS

Another rise in new vehicle sales and a further increase in lease penetration rates pushed new lease originations to their highest level ever in 2015, at just shy of 4 million units.

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No longer is leasing just for luxury models; the most leased vehicle in 2015 was the Honda Civic.

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Ideally, lease customers should fall into the higher credit tiers, and for the most part, they do. In the third quarter of 2015, 75 percent of all lessees were either in the prime or super prime credit tiers.

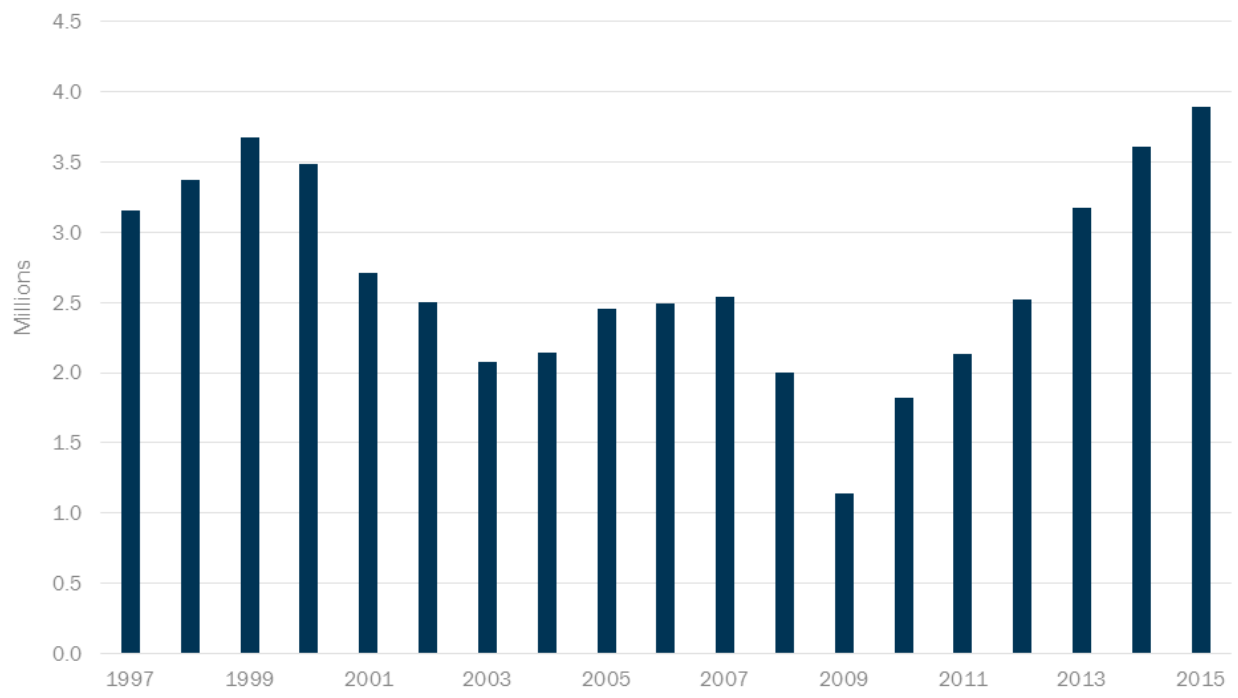
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The sheer number of off-lease units could pose a challenge to remarketers in future years. The key will be the level of subvention entailed in the original lease.

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In 2002, the last peak in off-lease volumes, CPO sales were only 38 percent as big as total off-lease volumes. In 2015, CPO sales and off-lease volumes were basically identical.

NEW VEHICLE LEASE ORIGINATIONS



Source: Manheim Consulting

**NEW LEASE ORIGINATIONS REACH RECORD LEVEL IN 2015**

Another rise in new vehicle sales and a further increase in lease penetration rates pushed new lease originations in 2015 to their highest level ever—just shy of 4 million units. New lease originations last year were 2.8 million higher than during the cyclical trough in 2009. Although some banks have carved out a niche in the retail consumer lease market, the overall industry is very much dominated by the captive finance companies.

From the recession low, lease penetration rates for GM, Ford, and Chrysler products have risen the most. Their lease penetration rates are now close to the industry average after falling to the low single digits in 2009. Major Japanese brands have also kept pace with the overall increase in lease penetration rates. And Hyundai/Kia, relatively new to leasing, went from a 2 percent lease rate in 2009 to 25 percent last year. In the luxury segment, lease penetration rates have always been more than twice the overall industry average. But, one key trend that has emerged in leasing over the past decade is that it has gone more mainstream—no longer is leasing just for luxury models. For example, the most leased vehicle in 2015, according to Experian, was the Honda Civic.

LEASE PENETRATION RATES BY MANUFACTURER

	2009	2014	2015
FCA	3.0%	19.1%	20.7%
Ford	5.4%	22.0%	23.8%
GM	2.1%	22.9%	25.3%
Honda	19.1%	30.5%	31.6%
Toyota	15.9%	25.6%	28.6%
Hyundai/Kia	1.9%	22.3%	25.3%
BMW	50.9%	54.2%	59.6%
Mercedes-Benz	46.4%	53.2%	53.8%
<b>Total Industry</b>	<b>13.2%</b>	<b>25.7%</b>	<b>28.0%</b>

Source: J.D. Power and Associates

### AN IMPROVED LEASING MODEL

The previous peak in leasing in 1999 was “leasing done wrong”: the wrong car (the one that couldn’t be retailed), the wrong customer (the one who couldn’t get financed), the wrong residual (guidebooks were overly optimistic, and that residual was bumped another 5 points or more in the lease contract), and the wrong remarketing process (or, to be honest, there was no remarketing process at all). Today, for the most part, we have “leasing done right”: the right car (one the lessor wants to get back), the right customer (one who wants to trade on a regular cycle and wants to avoid the residual risk entailed in a long-term finance contract), the right residual (analysts have become better forecasters, and when residuals are subvented, lessors often hold reserves), and the right remarketing process (a holistic approach that is planned in conjunction with the origination process).

As new vehicle sales become increasingly skewed to high-income households, it is only natural that lease penetration rates have risen. That’s because these are the very households that want to trade on a short, and regular, cycle. Putting this type of customer into a 72- or 84-month loan may garner near-term profits, but it will breed long-term customer dissatisfaction. Remember,

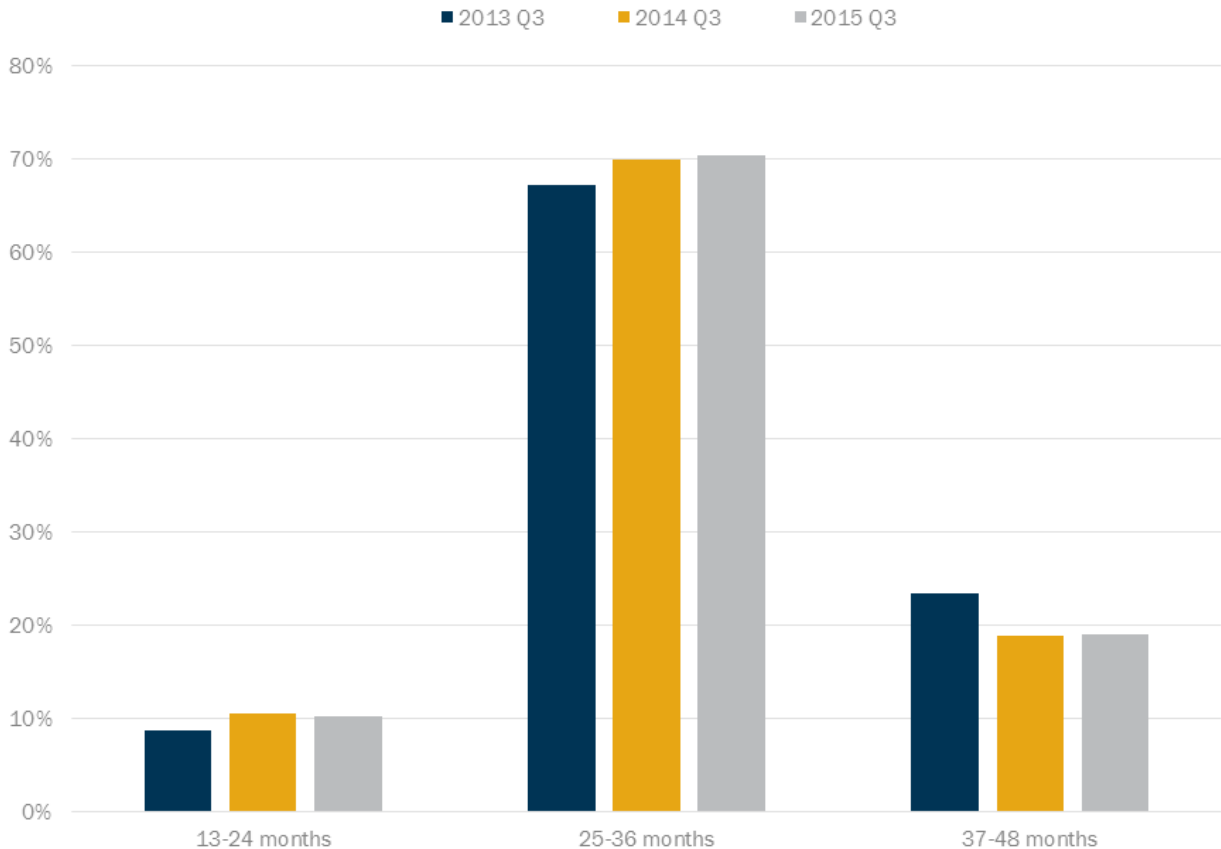
residual risk is present in all transactions—whether it is a retail finance contract, lease, or cash deal. It is just a difference of who holds that residual risk.

### THE RIGHT LEASE CUSTOMER AND THE RIGHT TERM

Ideally, lease customers should fall into the higher credit tiers—and, for the most part, they do. In the third quarter of 2015, 75 percent of all lessees were either in the prime or super prime credit tier, and their average FICO score was 715. For new vehicle buyers in a retail finance contract, only 70 percent were in the prime or super prime category, and their average FICO was 710. That sounds good and makes sense; but when Experian looked at the average FICO between loans and leases for individual models, they generally found lower FICOs for the leases. That’s not good. Leasing should never be used to simply move metal or put customers in a vehicle they can’t otherwise afford.

Likewise, in most cases, the term of a lease should be for three years or less. On that front, the industry is holding true, despite lengthening maturities for retail loans. The bulk of new vehicle leases continue to have a term between 25 and 36 months, according to Experian.

TERM DISTRIBUTION FOR NEW LEASE ORIGINATIONS



Source: Experian

**LEASING AND THE NEW VEHICLE SALES CYCLE**

An inherent risk in leasing (from the lessors’ standpoint) is that originations will generally peak at the top of the economic cycle, meaning that peak off-lease volumes will come back in a less favorable retail environment—and maybe even during a recession. Hence the importance of never aggressively subventing leases at the top of the cycle and of building reserves throughout the cycle.

But the fact that maximum lease returns may occur in a weak retail environment could be viewed as a positive if it helps moderate the new vehicle sales cycle. New vehicle sales have always been subject to large peak-to-trough swings (typically 25 percent to 33 percent—and during the Great Recession 42 percent), but a high volume of off-lease returns could reduce the magnitude of those swings. End-of-term customers are forced back into the market regardless of economic conditions. If they are satisfied customers whose financial condition has not materially changed (and for many, it won’t have changed since lessees are skewed to high-income households), they will lease another new vehicle. Had they been in a retail finance contract, they would have been more likely to remain on the sidelines until the overall economic environment improved. Securing these additional new vehicle sales, as well as supporting the dealer network (and themselves) with potential CPO sales, should be a partial offset to some of the pain of end-of-term residual losses experienced by lessors.

**RETURNING LESSEES WILL SUPPORT NEW VEHICLE SALES**

Pent-up demand was the principal driver of new vehicle sales increases in the initial stages of this recovery. But, by definition, that is not a long-term, sustainable force. We are now beginning to transition to a market supported by returning lessees, and not just any type of lessee—a satisfied one. From a dealer’s perspective, that’s pretty much automotive retailing’s utopia—happy customers returning on a regular cycle.

The current bifurcation in the retail finance market – high lease penetration rates as well as a lengthening in retail contract maturities—could be a good thing if dealers and salespeople correctly put the right customer into the right finance option. The higher lease penetration rate will help offset some of the lengthening in the trade cycle that naturally occurs with longer-term loans.

That said, the sheer volume of new lease originations (now approaching 4 million per year) could pose a challenge to remarketers in future years. The key will be the level of subvention entailed in the original lease. When not overly subvented at origination, a lease return is viewed by the lessor and grounding dealer as an opportunity to sell a satisfied customer another car. But if overly subvented, that lease return can start a downward spiral in both residual values and customer satisfaction.

**OFF-LEASE VOLUMES WILL RISE SIGNIFICANTLY**

Given the growth in new lease originations, we can be assured of a steady rise in off-lease volumes. And since the increases in lease penetration rates were not consistent across manufacturers, neither will be the changes in off-lease volumes. Note, for example, that although total lease originations in 2015 were more than three times higher than in 2009, new lease volumes have grown by a factor of 15 or more at GM, FCA, and Hyundai/Kia.

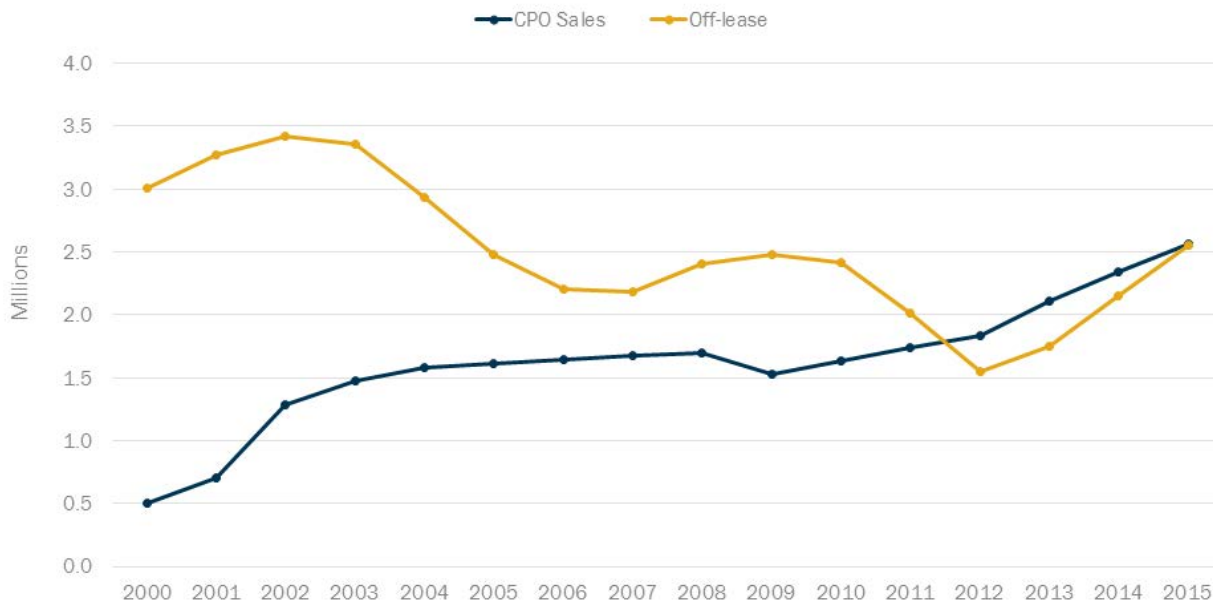
It will be challenging for the industry to absorb these off-lease volumes without producing large residual losses. All of these off-lease units will have to be subsequently retailed in the used vehicle market—and in short order, at a profit—so the question is: To what level will prices in the wholesale market need to adjust to effectuate these transactions? The needed residual adjustments in 2016 will likely be manageable, if the units come back into what we assume will continue to be a favorable retail market.

**OFF-LEASE VOLUMES—FURTHER GROWTH AHEAD**



Source: Manheim Consulting

OFF-LEASE VOLUMES VS. CPO SALES



Source: Manheim Consulting and Automotive News

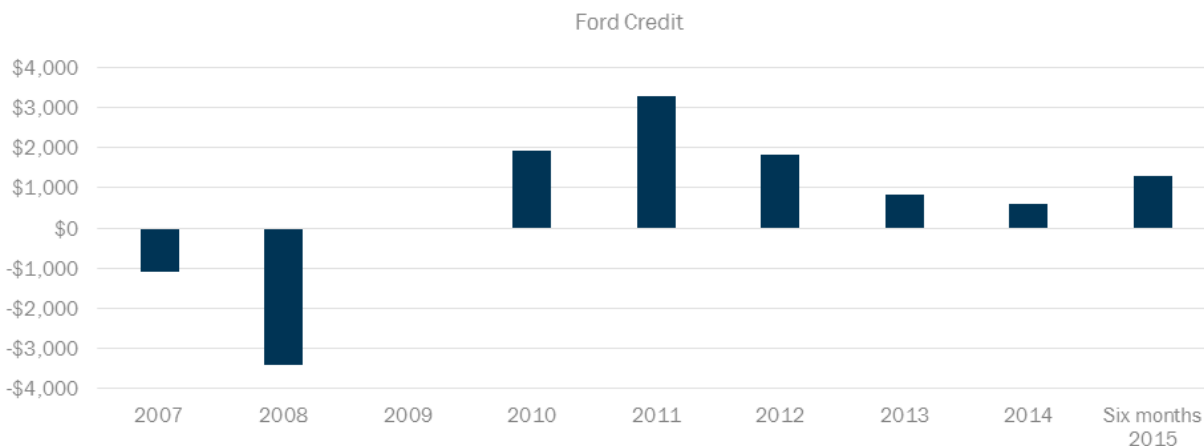
**OFF-LEASE VOLUMES AND CPO SALES ARE BENEFICIALLY LINKED**

End-of-term vehicles are generally a perfect fit to be sold as CPO units. In turn, CPO sales help support wholesale values and thus mitigate the lessor’s residual risk. And the lessor has opportunities to further moderate the residual risk by providing additional marketing muscle or incentives (like reduced-rate financing) behind the CPO programs. In 2002, during the last peak in off-lease volumes, CPO sales were only 38 percent as big as total off-lease volumes. In 2015, CPO sales and off-lease volumes were basically identical.

**END-OF-TERM GAINS MAY SOON DISAPPEAR**

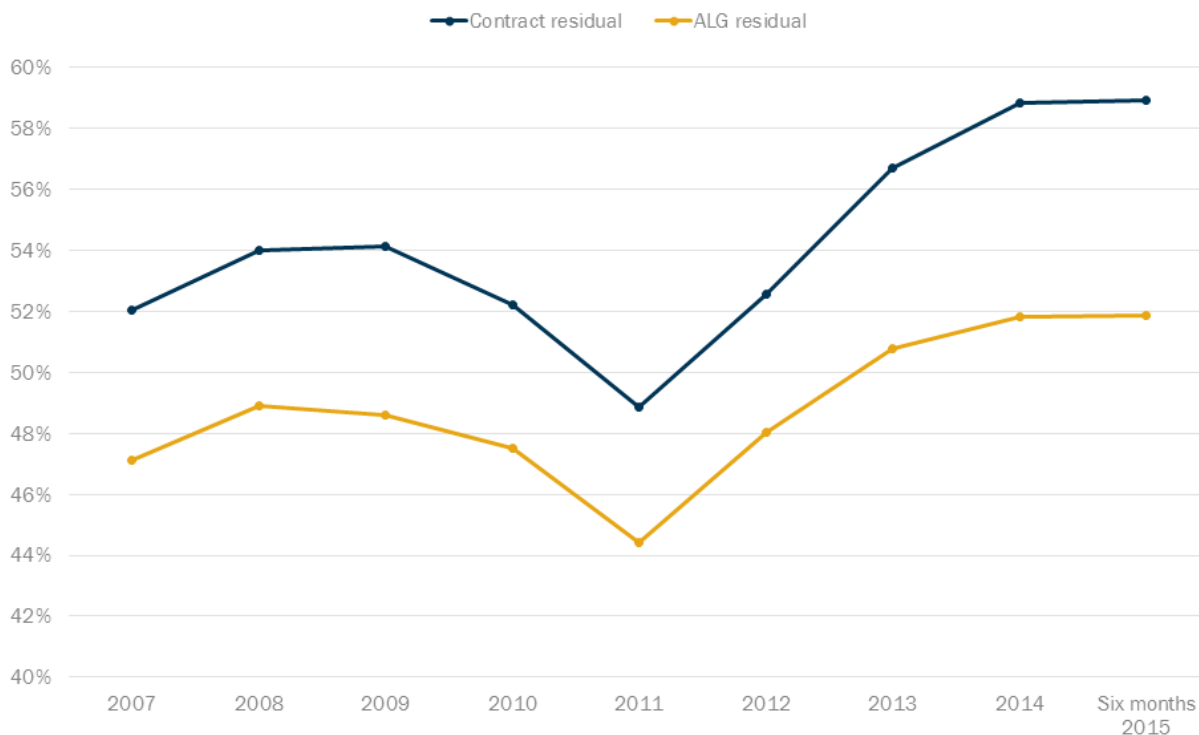
Lease remarketers are well-accustomed to cyclical swings in their portfolio performance. For example, they went from large losses on end-of-term units in 2008 to record gains on units sold in 2011. End-of-term gains have remained in place up until now, but they have shrunk. They will likely vanish in 2016. (There are no aggregated data on the performance of all lease portfolios; but the nearby graphic, depicting results for Ford Credit, gives an indication of industry trends.)

AVERAGE GAIN OR LOSS ON LEASE RETURNS



Source: SEC filings

CONTRACT RESIDUALS VS. ALG RESIDUALS — FORD CREDIT LEASES AS % OF MSRP



Source: Ford Credit Auto Lease Trust 2013-B

When wholesale prices were at their lowest in 2008, lease return rates were often well above 80 percent. As wholesale values reached new highs in 2011 and 2012, return rates fell well below 50 percent. With off-lease volumes rising in future years, and wholesale prices likely falling, lease return rates should begin to creep back up.

to used vehicle values. When wholesale prices were at their lowest in 2008, lease return rates were often well above 80 percent. As wholesale values reached new highs in 2011 and 2012, return rates fell well below 50 percent. With off-lease volumes rising in future years, and wholesale prices likely falling, lease return rates should begin to creep back up; but it is unlikely they will approach earlier highs. That's because lessors have a greater variety of tools (both carrots and sticks) to help, and entice, grounding dealers to purchase a reasonable share of returning units.

Expected, as well as contract, residuals have risen during the recovery—and the spread between the two has widened.

As noted before, these swings in portfolio performance are an inherent, and unavoidable, risk contained in the lease business model. New lease originations generally peak at the top of the economic cycle when residual value projections are lofty (since they are based, in large part, on past experience). That means that the peak in off-lease volumes will often come back during an economic down cycle when used vehicle valuations are low. Swings between gains and losses are also amplified by the fact that lease return rates (i.e., the share of off-lease units not bought by either the lessee or grounding dealers) are strongly and inversely correlated

**OFF-LEASE REMARKETING PRIORITIZES THE GROUNDING DEALER**

All captive finance companies, as well as the major independents, utilize at least one Internet upstream platform that offers end-of-term vehicles to an ever-widening audience of dealers prior to sale at physical auction. And those technologies, platforms, and processes have improved significantly in recent years.

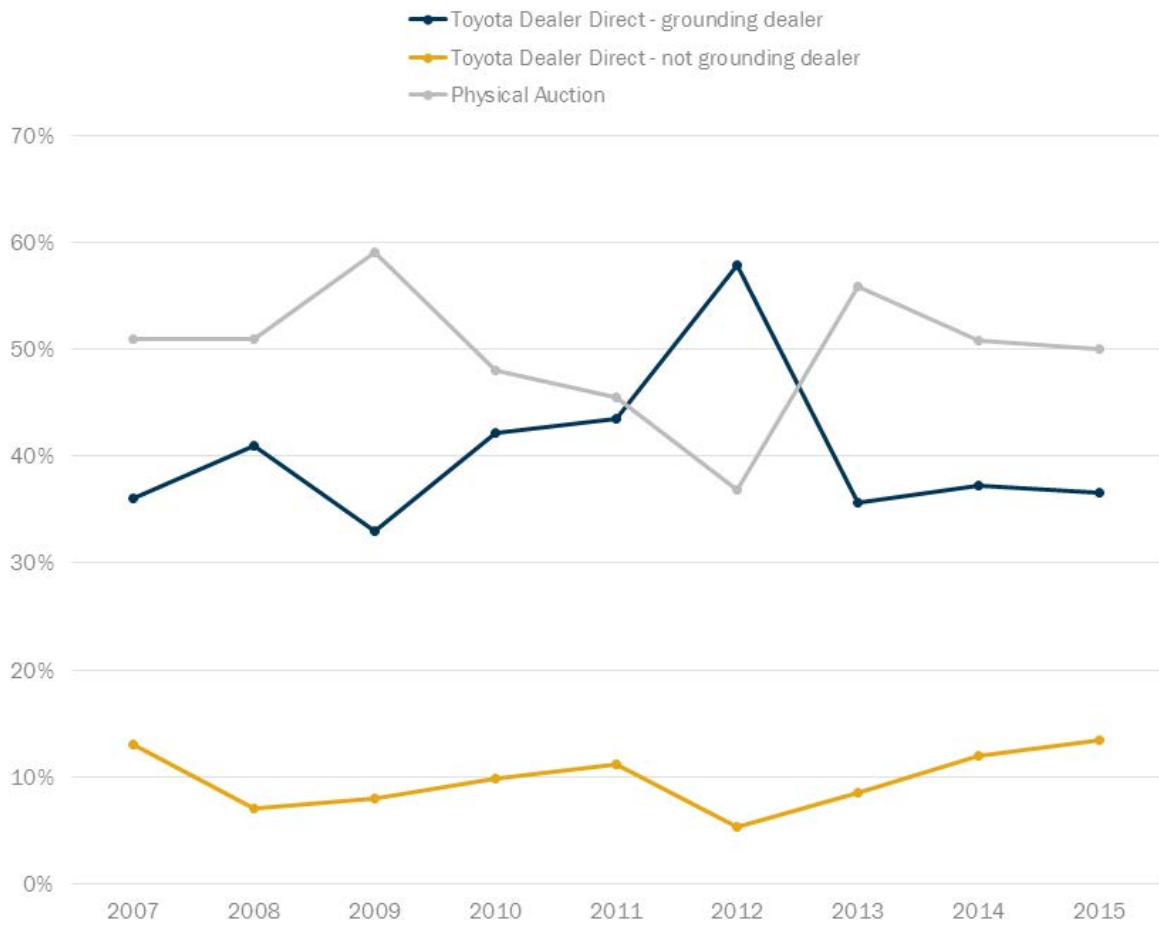
Most of the captives are using these technologies to keep a large share of the returning lease volume within



their dealer network—and, most notably, the grounding dealer. As off-lease volumes grow in coming years, it is likely that the share of off-lease units bought by the grounding dealer will decline, but probably not by much since the captive lessor will still put priority on that first possible sale—and offer an attractive price to achieve it.

The share of Toyota Financial Services’ off-lease units sold at physical auction declined from 59 percent in fiscal year 2009 (height of the recession) to 37 percent in 2012 (height of used vehicle values). The auction share has since returned to 50 percent.

**DISTRIBUTION OF TOYOTA FINANCIAL SERVICES OFF-LEASE SALES IN U.S.**  
(PERCENT OF TOTAL — FOR FISCAL YEAR ENDING 3/31)



Source: Toyota Financial Services SEC filings

2016 USED CAR MARKET REPORT

# REPOSSESSIONS

## 2015 HIGHLIGHTS

The auto finance market topped \$1 trillion in loans outstanding in 2015.

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Due to the different trajectories for homes and autos, mortgage obligations (by far the biggest component of household debt) remain 11 percent below the peak reached in 2008.

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On the new vehicle side, the top 10 lenders control 60 percent of the market, but on the used vehicle side, the top 10 lenders account for only 30 percent of all financing.

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The share of auto loan originations accounted for by people with a risk score below 620 (i.e., subprime) grew from 17.1 percent in the third quarter of 2010 to 22 percent in the third quarter of 2015.

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The number of auto loans seriously delinquent rose from 2.85 million in the third quarter of 2014 to 3.3 million in the third quarter of 2015.

### RETAIL CREDIT: THE GOOD TIMES KEEP ROLLING

There is nothing more important to the vitality of the new and used vehicle markets than the availability of retail financing. Little wonder then that near-record new vehicle sales and record used vehicle profits came hand-in-hand with an auto finance market that topped \$1 trillion in loans outstanding in 2015. With both loan rates and delinquency rates at historic lows, these are good times for lenders, dealers, and consumers.

*But, given that credit runs in cycles, how long will the good times last? Or more specifically:*

- Will interest rate hikes end the party?
- Will lenders become overly aggressive?
- Will the CFPB over-regulate?
- Will borrowers take on more than they can afford?

Let's look at the story of auto financing in 2015 to find the answers to these and other questions.

### AUTO ABS ISSUANCE TOPS \$100 BILLION IN 2015

There's an old saying in the industry that the availability of credit is more important than the cost of credit. And it's true. In a near-zero interest rate environment, there is naturally a desperate search for yield, and auto loans provide that yield with little relative risk to investors. Witness the growth in the ABS market for auto loans.

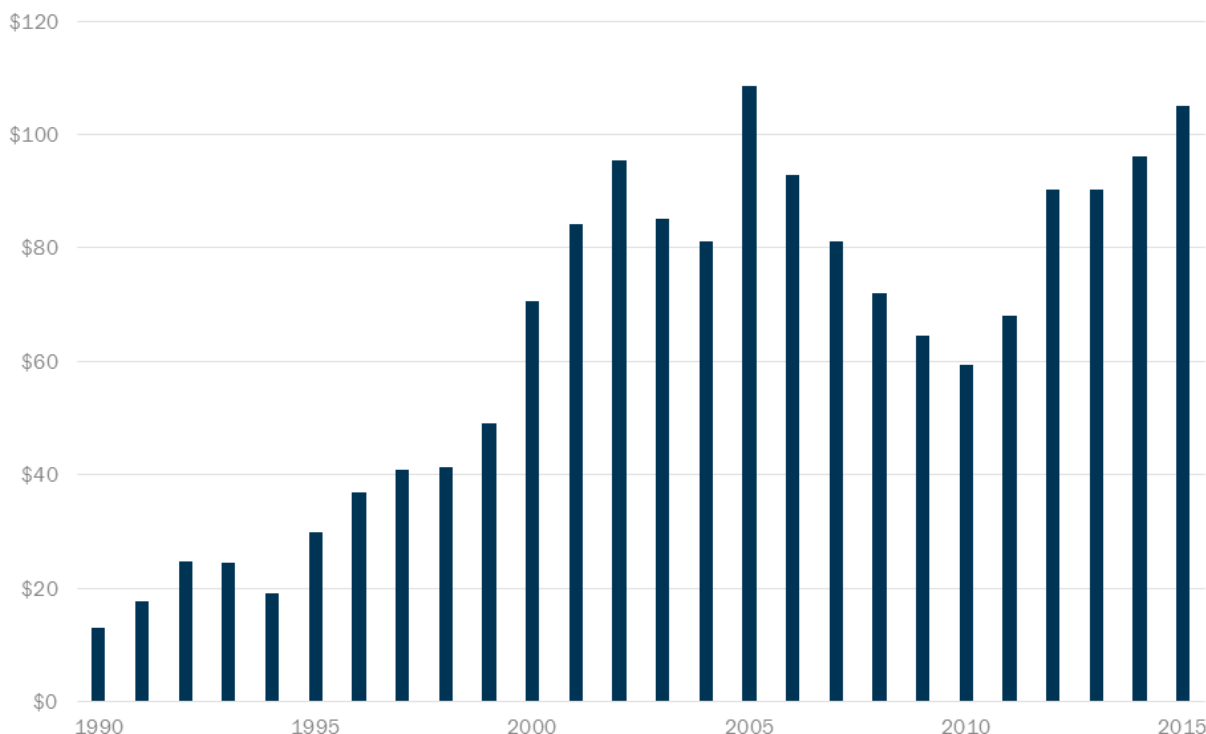
Asset-backed securitization issuance in the automotive market totaled over \$90 billion in 2012, 2013, and 2014—and then, in 2015, issuance topped \$100 billion for only the second time ever. The higher issuance has come even as many large banks relied heavily on deposit-backed funding for auto loan originations. The terms of the securitization deals (for example, the amount of over-collateralization needed to achieve a given credit rating) were favorable to issuers, and investor interest in these instruments has remained high. Recently, some deal terms became a little tougher, and some lenders set aside larger loss reserves, but this simply represents an efficient market correcting itself.

### AUTO LOANS OUTSTANDING SURPASS \$1 TRILLION

The dollar amount of auto loans outstanding rose above \$1 trillion in mid-2015 and by year-end stood at \$1.1 trillion, according to data from the Federal Reserve Board Bank of New York. In each of the past three years, auto loan balances have grown at a double-digit pace, while household incomes grew only modestly. Typically, that would suggest consumers are becoming overextended and/or auto lenders are becoming overly aggressive, but neither is the case today.

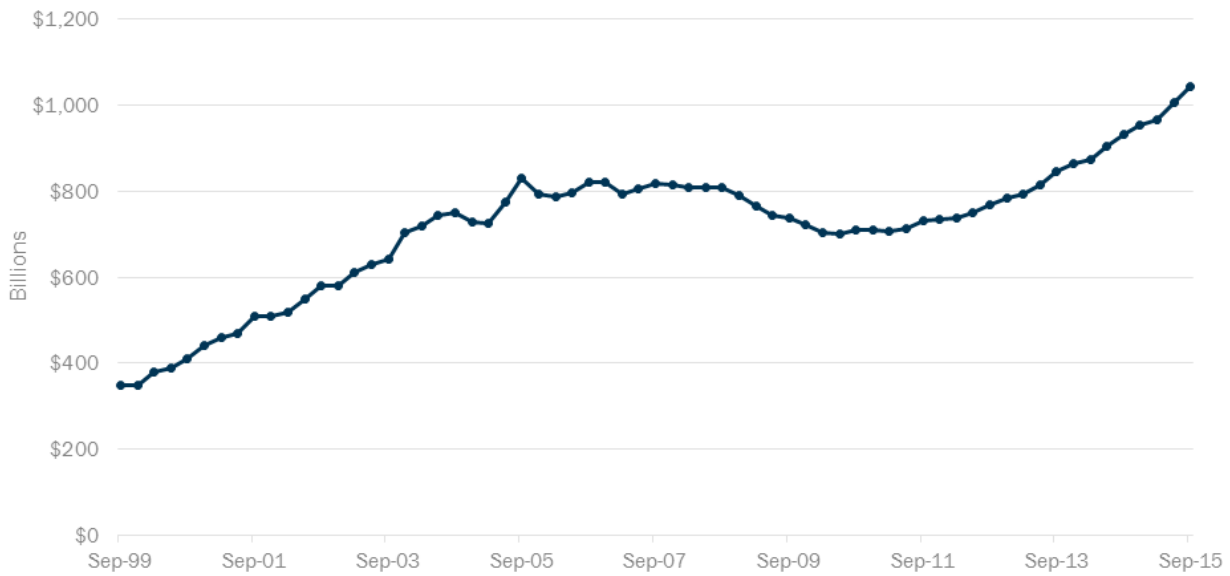
The growth in auto loans must be taken in the context of total household obligations. When that is done, it provides further evidence of how much the auto industry has outperformed other sectors of the

**AUTO ABS ISSUANCE BY YEAR**



Source: SIFMA

**AUTO LOANS OUTSTANDING**



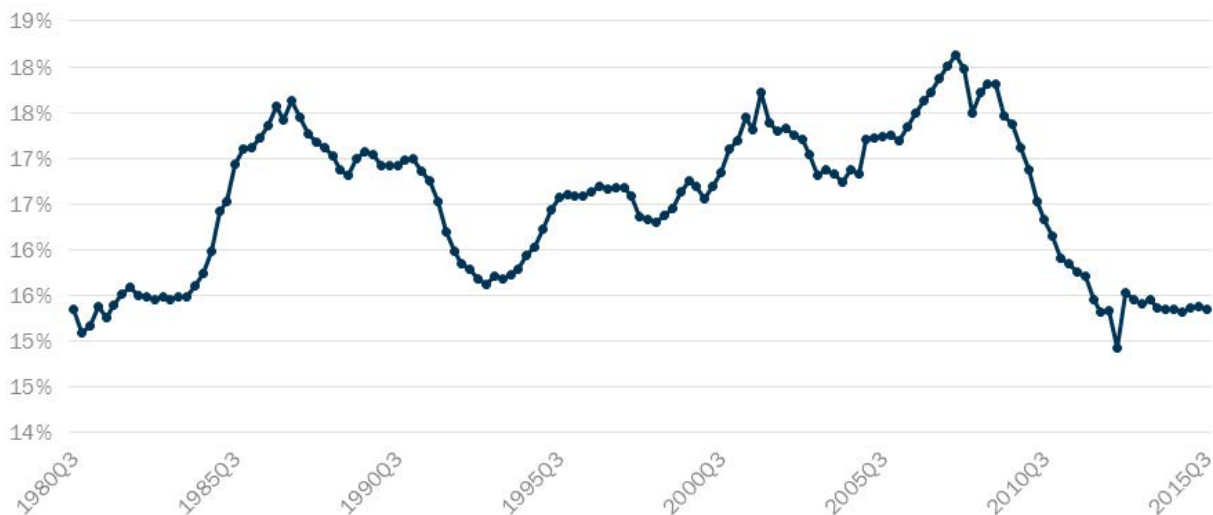
Source: Federal Reserve Bank of New York

economy. Due to the different recovery trajectories for housing and autos, mortgage obligations (by far the biggest component of household debt) remain 11 percent below the peak reached in the third quarter of 2008. Credit card debt also remains below its previous peak. Add in low interest rates, and you find that the Financial Obligation Ratio (the sum of mortgage, rent, auto lease and loan, and property tax payments as a percent of disposable personal income) is currently running at its lowest level in 30 years.

**AUTO DELINQUENCIES AND DEFAULT RATES REMAIN AT HISTORIC LOWS**

The lighter debt load relative to income partially explains why borrowers have been able to keep current on their auto loans, but the real difference in recent years has been the shift in labor market conditions. To be sure, wage growth has been weak and the share of employment accounted for by part-time workers has grown; but those are factors that workers are aware of, and can account for, when taking out

**FINANCIAL OBLIGATION RATIO**  
TOTAL HOUSEHOLD MORTGAGE, RENT, AUTO LOANS & LEASES, AND PROPERTY TAXES AS % OF DISPOSABLE PERSONAL INCOME



Source: Federal Reserve Board



their loans. What they can't account for is unexpected job loss, which is the No. 1 reason for credit default. In 2015, job security — as measured by initial jobless claims adjusted for employment — was at its highest level ever.

Low gas prices are another factor that has kept loan delinquencies low, especially in the subprime tiers. That's because pump prices are another cost that can unexpectedly hit household budgets — either favorably or unfavorably. Given this, it is not surprising that the S&P Auto Credit Default Index remains at historic lows, despite ticking up in the latter part of 2015.

### GIVING CREDIT WHERE CREDIT IS DUE

The auto lending market is a competitive landscape with many players, ranging from large money center banks to small independent finance companies. Some lenders provide loans across all credit tiers, while others focus on particular niches. Some lenders make direct loans to consumers, but many more make indirect loans through dealers. Some lenders are national; many more are local. The end result is an industry that efficiently, and cost-effectively, funds new and used vehicle buyers of all credit types — in other words, "giving credit where credit is due."

Another byproduct is an industry with low levels of lender concentration. On the new vehicle side, the top 10 lenders control 60 percent of the market; but on the used vehicle side, the top 10 lenders account for only 30 percent of all financing. As a result, there are many banks, finance companies, and credit unions with small auto loan portfolios and, thus, few repossessions. This has created an opportunity for third-party providers to handle the collateral collection and remarketing needs of these lenders.

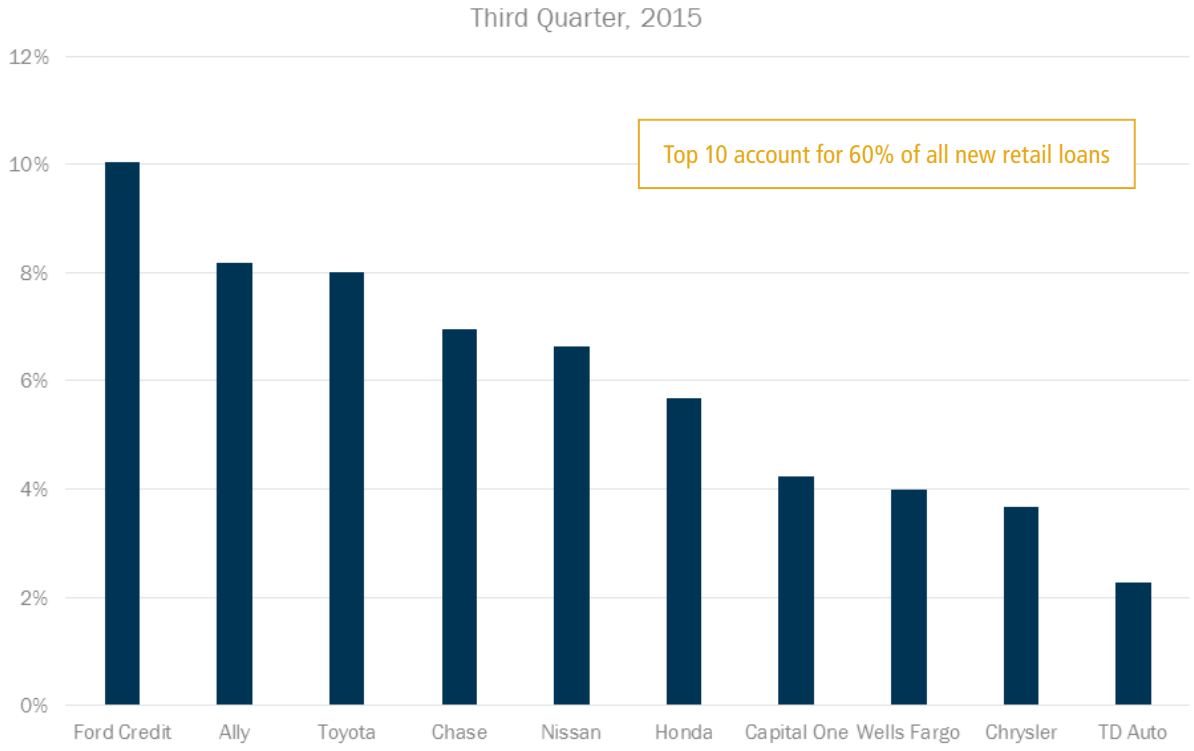
### THE LOOMING ISSUE OF LONG-TERM LOANS

In a period of just two years, the share of used vehicle loans with a term of 61 months or more grew from 51.1 percent to 57.5 percent. Currently, 16.2 percent of all used vehicle loans are for a term of 73 to 84 months, up from just 12.3 percent in 2013. The prevalence of long-term loans is, of course, even higher for new vehicle financing, where 72-month contracts have become the new norm.

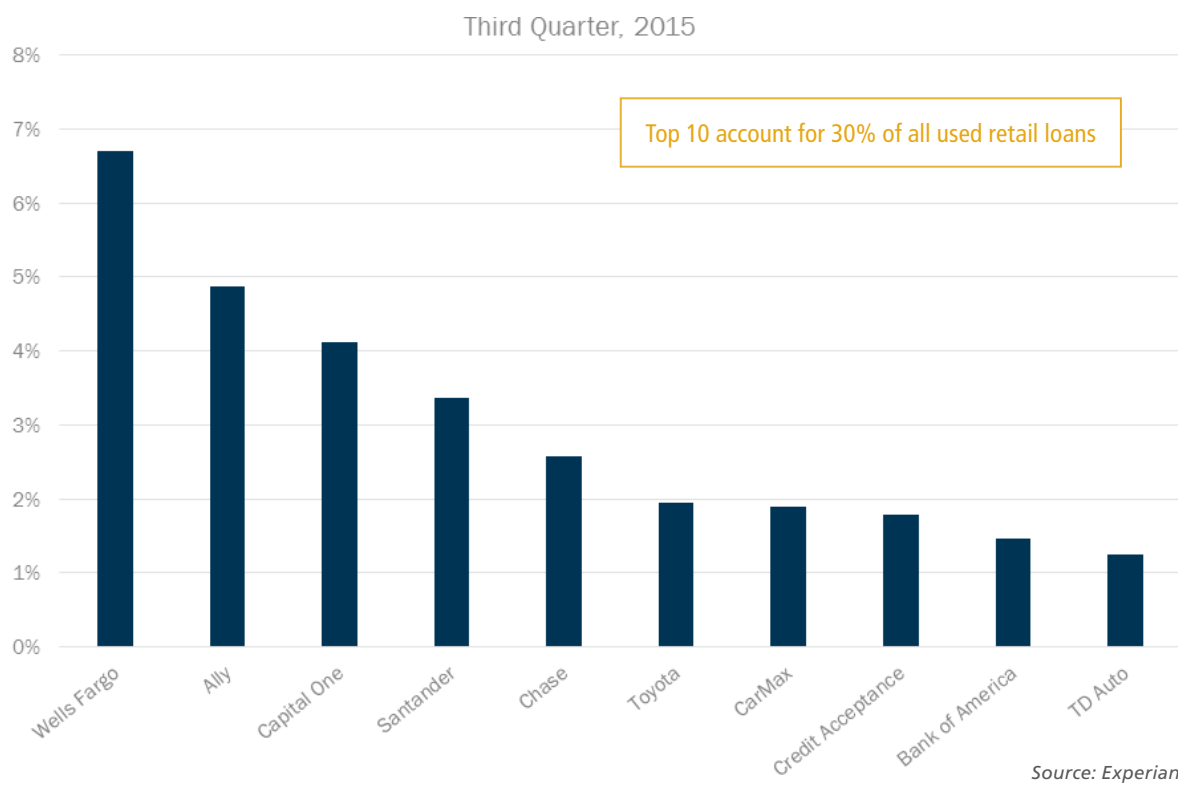
Lenders report that longer loans, in and of themselves, do not materially impact repossession rates. That may be true, but it is inarguable that longer loans increase the severity of loss on credit defaults. And, since the equity point is reached further out in long-term contracts, it is reasonable to expect that a greater number of repossessions will take place further out in the contract. This can be especially problematic in the lower credit tiers. These are households that by definition are living on the edge. Unfortunate events such as illness, divorce, or job loss can quickly push them into default, and of course, with the longer loan, the odds that a bad event will occur at some point during the term increases. But, even for the higher credit tiers and the vast majority of loans that never go delinquent, longer-term contracts can pose a problem — customer dissatisfaction. That's because many owners will find it expensive, or impossible, to trade out of their current vehicle at the time they would like.

Lenders and dealers can mitigate some of the issues of longer-term loans by securing more upfront money. In reality, however, the opposite is occurring as loan-to-value ratios have generally risen. But again, lenders are comfortable with this given the exceptionally low level of delinquencies.

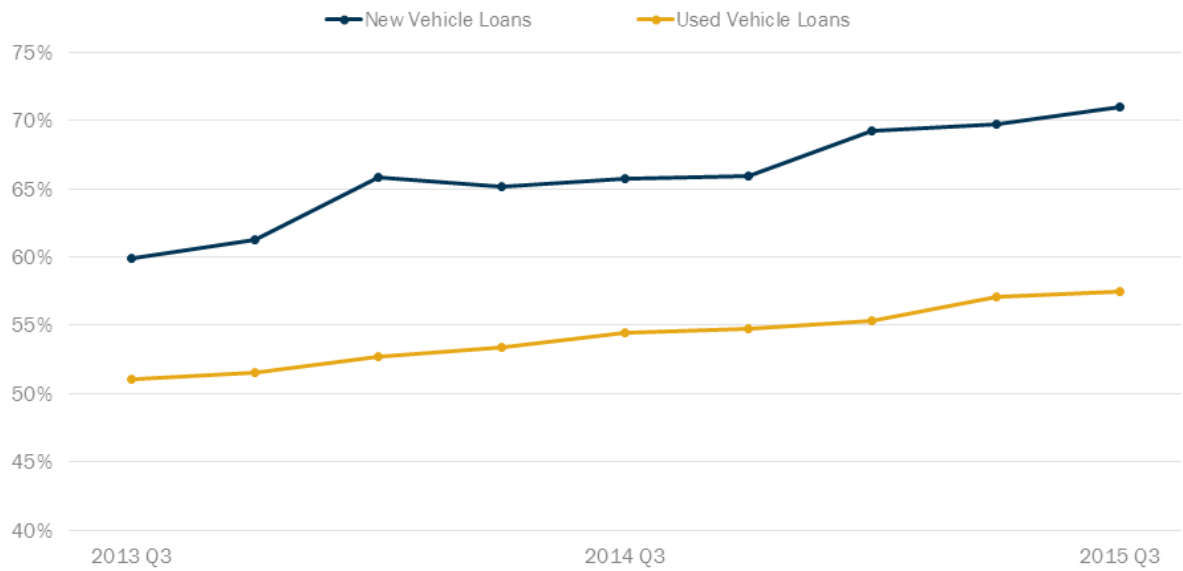
**NEW RETAIL LOAN MARKET SHARE**  
TOP 10 LENDERS



**USED RETAIL LOAN MARKET SHARE**  
TOP 10 LENDERS



SHARE OF AUTO LOAN ORIGINATIONS WITH A TERM OF 61 MONTHS OR MORE



Source: Experian

**SUBPRIME RECAPTURES NORMAL SHARE OF THE AUTO LENDING MARKET**

The share of auto loan originations accounted for by people with a risk score below 620 (i.e., subprime) grew from 17.1 percent in the third quarter of 2010 to 22.0 percent in the third quarter of 2015, according to data from the Federal Reserve Bank of New York. At the height of the last lending cycle, subprime accounted for approximately 30 percent of all auto lending. Given where we are in the economic cycle, it is not surprising

that these subprime auto loan originations are performing extremely well. Many of today’s subprime borrowers have very reasonable debt-to-income ratios; it’s just that their credit scores were dinged during the recession.

**REPOSSESSION VOLUMES GROW MODESTLY**

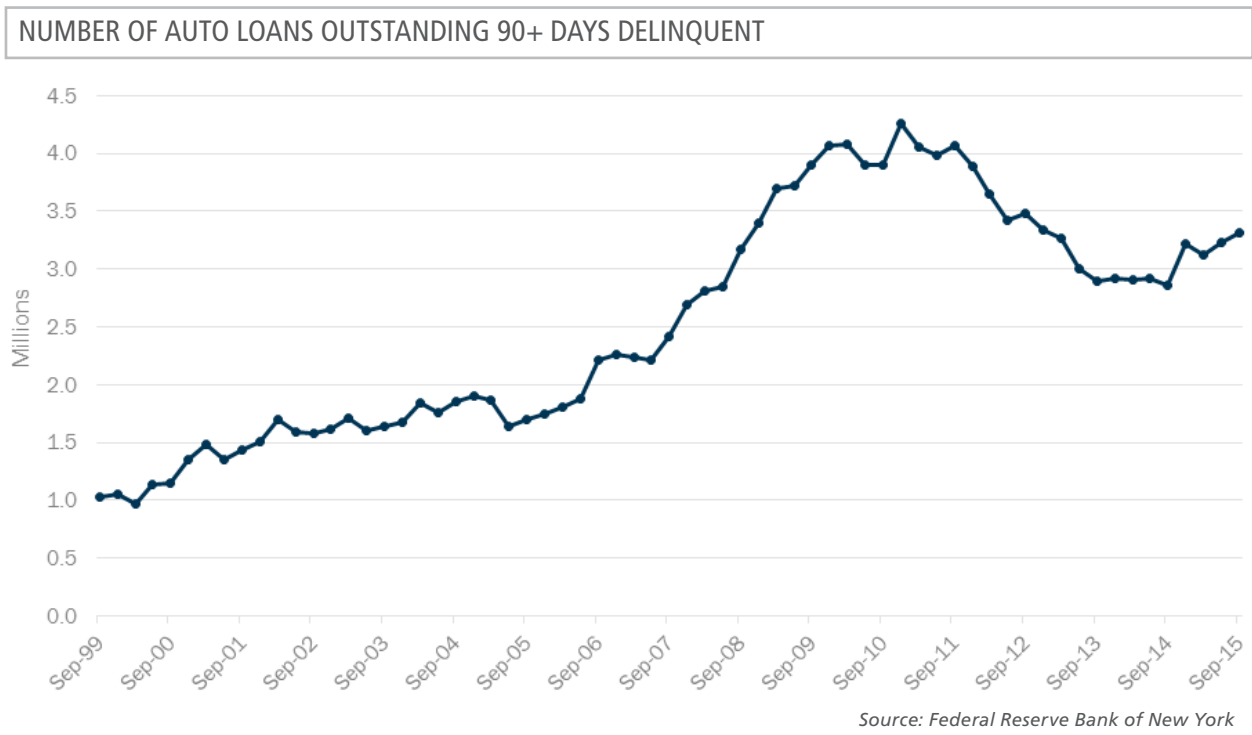
Despite exceptional portfolio performance, repossessions—and potential repossessions—continue to grow simply because of the larger number of contracts outstanding.

SUBPRIME AS SHARE OF AUTO LOAN ORIGINATIONS



Source: Federal Reserve Bank of New York





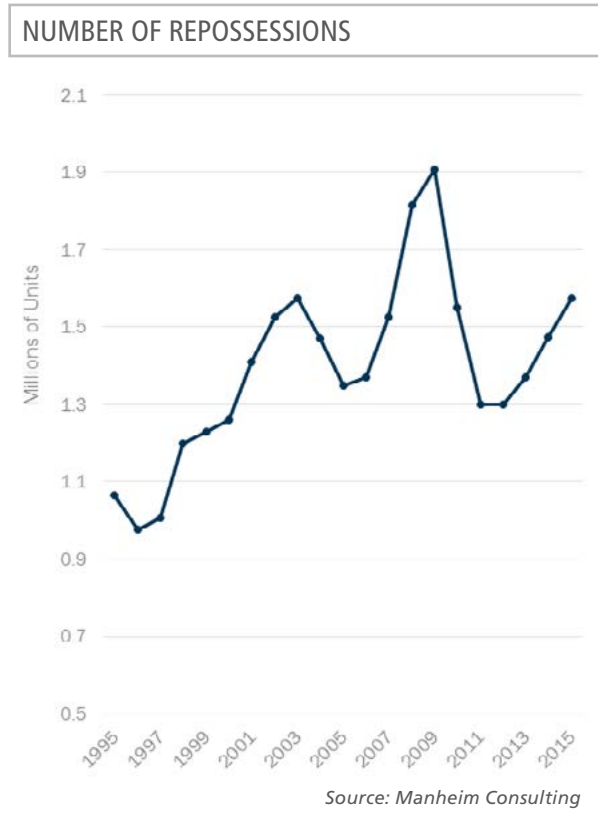
Note for example that, although the seriously delinquent rate for auto loans (90-plus days) has been flat in recent years, the actual number of seriously delinquent accounts has been rising. Based on data from the Federal Reserve Bank of New York, the number of auto loans seriously delinquent rose from 2.85 million in the third quarter of 2014 to 3.3 million in the third quarter of 2015.

Given the number and credit tier distribution of contracts outstanding, the number of repossessions will grow in coming years even if the economic environment remains stable. It will take some time, however, to get back to the peak of 1.9 million repossessions reached in 2009.

**REPOSSESSION REMARKETING: QUICK CONVERSIONS FOR HIGH RETURNS**

Lenders are naturally focused on converting repossessed units into cash as quickly as possible. Various laws and regulations dealing with the processes of collateral collection and liquidation often present a stumbling block to that quick conversion, but lenders and their auction partners have been successful in streamlining the processes that they do control.

Given the lender’s strong focus on time-to-sale, they generally strive for, and achieve, high conversion rates. That, coupled with little or no reconditioning, means that wholesalers are often the buyers of repo units. Sometimes they will do some light cosmetic work and then re-wholesale the unit. That arbitrage should not be regarded as a lost opportunity for the seller, but rather simply the wholesale market’s efficiently getting vehicles to the ultimate end dealer in the condition desired.



2016 USED CAR MARKET REPORT

# FLEETS

## 2015 HIGHLIGHTS

New vehicle purchases by commercial fleets grew by more than 2 percent in 2015 to 629,000 units, the sixth consecutive yearly increase.

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Total commercial and government fleet purchases reached 871,000 in 2015, up considerably from the 588,000 purchased in 2009, but shy of the million-plus units bought in 2006 and 2007.

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Unlike rental cars, fleet purchases are concentrated within a few makes and models; the top five car models usually account for 40-50 percent of all the new cars registered to commercial fleets.

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After several years of increases, a straight average of commercial fleet auction prices declined slightly in 2015, driven primarily by weakness in the compact car segment.

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The midsize car segment of the commercial fleet market had a modest decline in pricing in 2015, despite having fewer miles at the time of sale. Nevertheless, the average auction price of a midsize fleet car remained above the overall auction average.

## NEW VEHICLE FLEET PURCHASES INCREASE FOR SIXTH CONSECUTIVE YEAR

New vehicle purchases by commercial fleets grew by more than 2 percent in 2015 to 629,000 units. It was the sixth consecutive yearly increase and pushed total purchases 81 percent higher than during the 2009 recession. New vehicle purchases by government agencies, however, declined slightly in 2015 and were little changed from their 2009 level. This brought total commercial and government fleet purchases to 871,000 in 2015, up considerably from the 588,000 purchased in 2009, but shy of the million-plus units bought in 2006 and 2007.

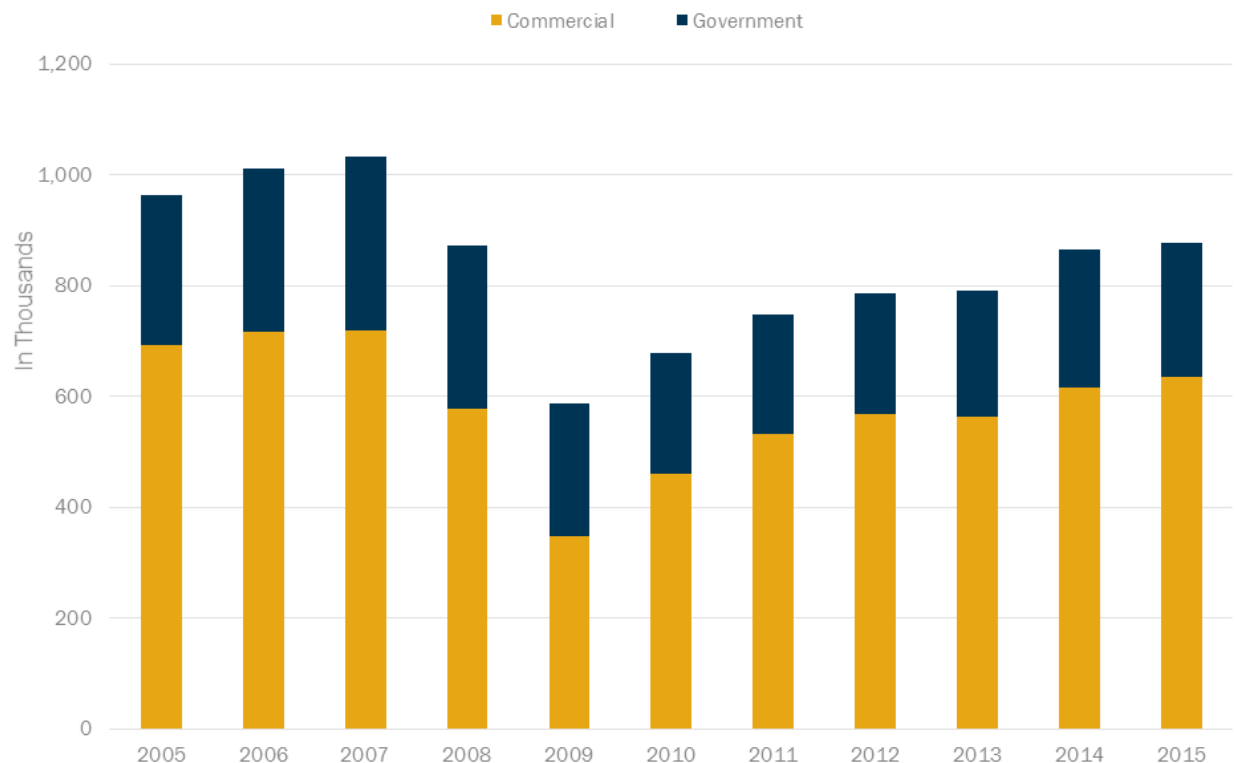
In 2016, commercial fleet purchases should continue to grow as a result of higher employment levels; but the increases won't be nearly as large as earlier in the cycle when businesses had both pent-up demand and the desire to "short-cycle" some of their fleets to take advantage of exceptionally high wholesale prices. Over the longer term, we see new vehicle sales into fleet staying below the 1 million mark as the result of employment shifts between industries, a changed occupational distribution within industries, a continued tight rein on both private and public fleet budgets, and a concerted effort to improve the utilization of the existing fleet. As such, future fleet sales will be driven more by the replacement cycle created by the 6.5 million vehicles currently operated by commercial entities and government agencies.

## FLEET OPERATING COSTS IMPROVE IN 2014

In 2015, fleet managers once again enjoyed stable or declining operating costs as a result of low energy prices, stable maintenance and repair expenses, and lower-than-expected depreciation costs. These savings were partially offset by safety recalls that increased rental outlays for supplemental units. Keeping operating expenses in check is important for the future health and growth of the fleet industry since budget outlays to the fleet department remain constrained. Lower operating expenses better enable fleet managers to grow units in operation and provide higher service levels to fleet drivers.

Today's higher-quality vehicles and, in some cases, extended powertrain warranties have kept fleet expenses in check by reducing maintenance and repair costs on a per-mile basis. When repairs do occur, however, they are significantly more expensive than in the past as the diagnosis is often more complex and the parts and labor costs higher. Similarly, the prevalence of synthetics has made oil changes more expensive, but it has lengthened service intervals. Additionally, fleet operators, like retail consumers, have benefited from manufacturer programs that cover first-year oil changes and tire rotation. But it remains important that fleet managers and fleet management companies ensure that all required fluid changes and scheduled services are actually performed and documented. Otherwise, warranty claims will be denied.

### NEW VEHICLE SALES INTO COMMERCIAL AND GOVERNMENT FLEETS



Source: Bobit Business Media

After years of significant increases, tire prices were stable in 2014 and 2015, primarily as a result of low oil prices, and thus, it is likely that tire prices will remain stable in 2016. The shift toward more expensive, larger-diameter tires appears to be a trend that has now played out, but there is increased use of special-sized tires for which there is not a lot of price competition between manufacturers in the replacement market.

One area of fleet operating expense that is bound to rise in coming years is funding costs. The Federal Reserve finally hiked the targeted federal funds by a quarter-point in December of 2015, and it is expected that there will be several more hikes over the course of 2016. Even with the increases, however, interest rates will still be low from a historical perspective.

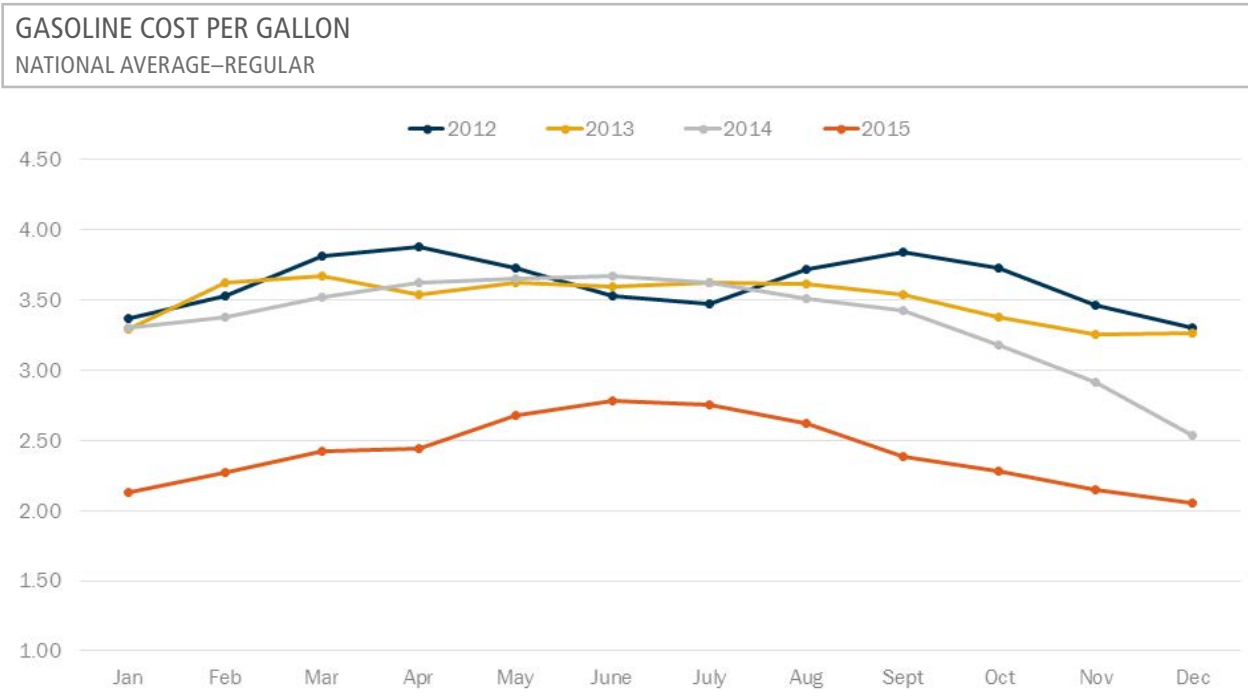
**FLEET FUEL EFFICIENCY CONTINUES TO IMPROVE**

Fleet managers have worked hard for many years to right-size the vehicles in their fleets to precisely meet needed requirements. After achieving the proper market class mix, they then strived to purchase the most fuel-efficient models and equip them with the proper options. This practice not only lowered annual fuel costs but, in many instances, also protected resale values, as consumer interest in fuel economy was also high in the used vehicle market. In 2015, however, this scenario did not play out as significantly lower gas prices shifted consumer preferences. In addition, strong price competition on the new vehicle side within the compact and midsize car segments further hurt residual values for these types of vehicles.

Even though current fundamentals suggest that pump prices will remain low, fleet managers will still work to increase the overall efficiency of their vehicle portfolio. After all, fuel costs are by far the largest operating expense in fleet budgets—and there is no guarantee that today’s lower fuel costs will persist or that gas taxes might not be raised. As such, fleet managers have been quick to adopt technologies that reduce fuel expense—for example, telematics that promote route optimization, reduce idling, and improve driving habits. Fleet managers have also benefited from the fact that new vehicles across the board have become more fuel-efficient. Although the average sales-weighted fuel economy of new vehicles sold in the U.S. declined in 2015, that was due to shifting sales between market classes. The fuel efficiency within a given market segment continued to rise.

Alternative fuel vehicles have often been placed in fleet service due to corporate sustainability dictates, not because of expected savings. In some instances, however, the higher number of miles driven by fleet vehicles enables them to show a positive payback that would not be possible for a typical retail user. For example, vehicles powered by natural gas already have a favorable total cost of ownership in some fleet situations.

But, in 2015, most alternative fuel vehicles, such as hybrids, suffered from both a higher acquisition cost and a faster depreciation rate. In addition, alternative fuel vehicles open up the fleet manager to greater residual risk since the end-of-service value is less predictable and subject to large short-term swings.



Source: Oil Price Information Services

## SALES-WEIGHTED MPG—NEW VEHICLE SALES



Source: University of Michigan Transportation Research Institute

### CONCENTRATED, BUT COMPLEX, BUYING DECISIONS

Unlike rental fleets, commercial and government vehicle purchases are generally concentrated within a few makes and models. Registration data from R.L. Polk shows that the top five car models usually accounted for 40–50 percent of all the new cars registered to commercial fleets (in the van and pickup segments, the percentage runs well over 80 percent).

Part of this concentration is a result of historic buying patterns geared toward domestic manufacturers that are fleet-friendly with respect to order-to-delivery times, custom up-fitting, and incentives. But, it also reflects the fleet manager's conscious decision to limit the number of models available to drivers on fleet selector lists.

More concentrated buying has not meant less complicated buying. In particular, the practice of staggered new model introductions throughout the year has made the fleet manager's task more difficult. It's impossible for the fleet manager to do model-to-model comparisons when the final specs of a potential buy have not yet been released. Furthermore, staggered new model introductions invariably lead to staggered purchasing and remarketing cycles, something the fleet manager would prefer to avoid. In 2015, as in prior years, February and March accounted for the highest share of new fleet deliveries.

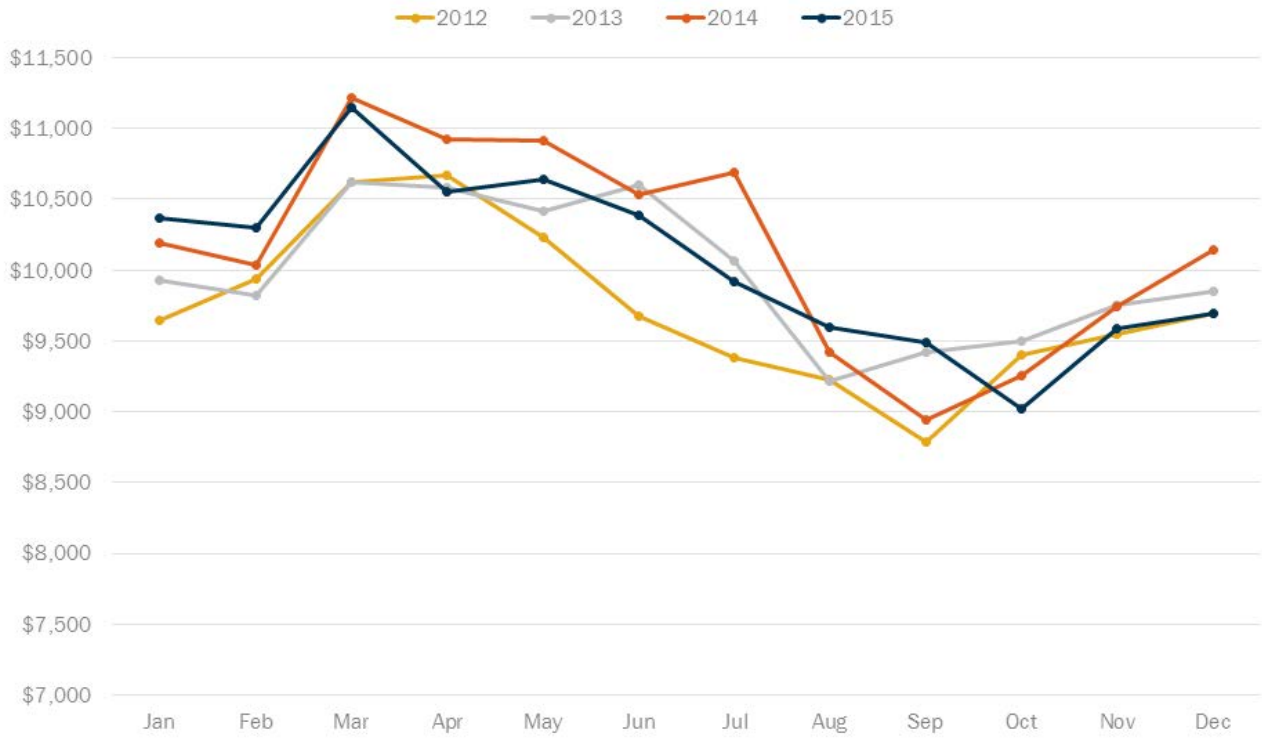
### FLEET RESALE PRICES REMAIN IN NARROW RANGE

After several years of increases, a straight average of commercial fleet auction prices declined slightly in 2015. This was driven primarily by weakness in the compact car segment. As in the overall market, pickups and vans enjoyed lower-than-expected depreciation. All market segments exhibited smaller seasonal swings in pricing during 2015.

The important midsize car segment of the commercial fleet market had a modest decline in pricing in 2015, despite having fewer miles at time of sale. Nevertheless, the average auction price of a midsize fleet car remained above the overall auction average. It used to be thousands less. That change occurred as auction sales shifted toward more dealer consignment sales, which are typically older, less-expensive units. With the average commercial fleet unit now priced right in the mix with many other types of auction units and sellers, the fleet reseller faces more competition in attracting buyers. Additionally, since the average wholesale price of a fleet unit has risen so much over time, it is important for fleet remarketers to recognize that their buyer base has also changed.

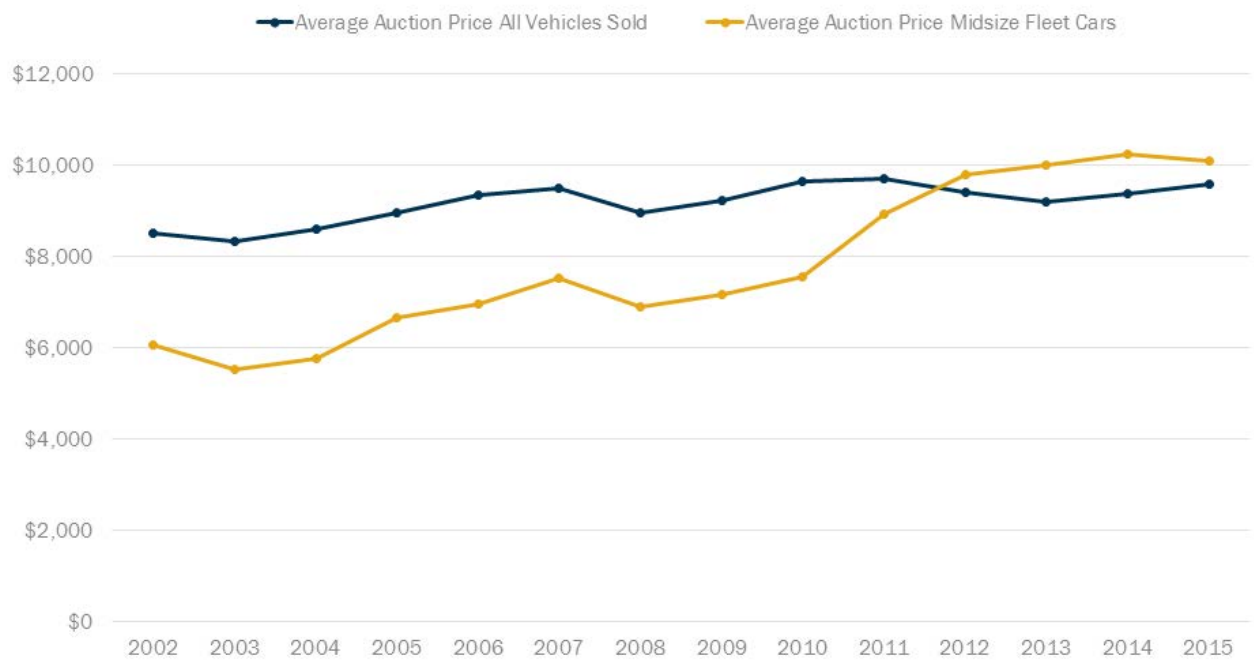
In 2011 and 2012 and, to a lesser extent, in 2013, fleet managers availed themselves of opportunities to cycle out of fleets early to take advantage of higher wholesale prices. Interestingly, at the same time, some

AVERAGE AUCTION PRICE  
MIDSIZE FLEET CARS



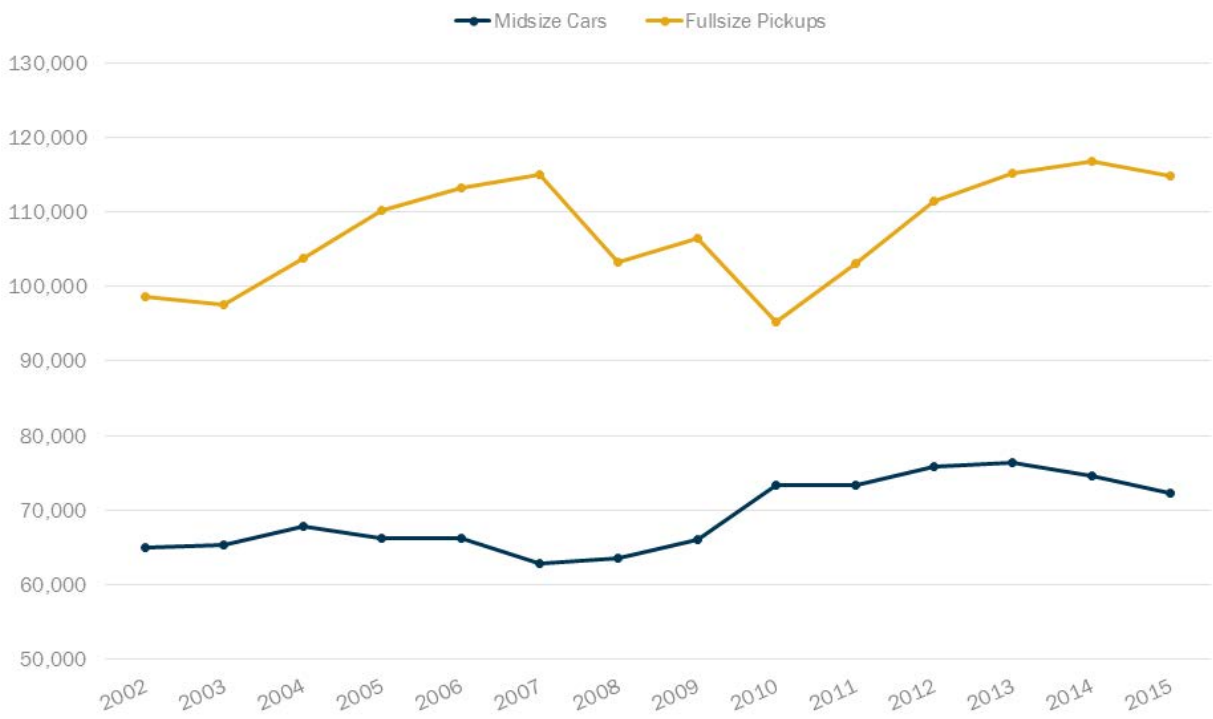
Source: Manheim Consulting

MIDSIZE CAR VS. OVERALL AUCTION AVERAGE



Source: NAAA & Manheim Consulting

**AVERAGE MILEAGE**  
COMMERCIAL FLEET UNITS SOLD AT AUCTION



Source: Manheim Consulting

The midsize car segment of the commercial fleet market had a modest decline in pricing in 2015, despite having fewer miles at time of sale. Nevertheless, the average auction price remained above the overall auction average.

fleets were extending the service lives of their vehicles. As a result, the mileage on fleet units being remarketed became more dispersed. In 2014 and 2015, patterns returned to normal.

For midsize cars, average mileage has moved down in the past two years; but it remains above 70,000 miles. Prior to the recession, average mileage was more likely to be in the 65,000-mile range. For pickup trucks, average mileage ticked down in 2015, but remained close to 115,000 miles.

**FLEET MANAGEMENT COMPANIES DRIVE REMARKETING IMPROVEMENTS**

Fleet management companies (FMCs) have been pioneers in using analytics to protect residual values. For example, studying the impact that various vehicle options have on resale value or determining the optimal service lives for particular types of vehicles.

FMCs have also been innovators as well as catalysts in moving the whole remarketing industry forward: for example, upstream selling and multiplatform listing.

All of this belies the common myth that fleet management companies are less interested in resale value since, generally, they do not carry the residual risk. The FMC/fleet manager client relationship, like most others in the remarketing world, is built on a true partnership working toward mutually beneficial goals.



TOP 10 FLEET MANAGEMENT COMPANIES  
U.S. VEHICLES IN 2014

	Vehicles Funded & Managed
GE Capital Fleet Services*	883,857
ARI	867,885
Element Fleet Management	470,000
Enterprise Fleet Management	390,000
LeasePlan USA	345,000
Wheels	303,900
Donlen	200,000
Emkay	92,000
Merchants Fleet Management	42,486
Mike Albert Fleet Solutions	40,150
<b>Total</b>	<b>3,697,462</b>

\*In August 2015, Element Financial closed on the acquisition of GE Capital's U.S.-based fleet operations.

Source: Automotive Fleet

2016 USED CAR MARKET REPORT

# SALVAGE

## 2015 HIGHLIGHTS

In 2015, the overall salvage marketplace experienced an increase in volume and moderate downward price pressure while overall demand remained strong.

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Total-loss vehicles experienced strong downward price pressure from a decrease in scrap metal prices.

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Salvage vehicles with light to moderate damage experienced only a slight year-over-year price drop.

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Actual cash values for total-loss vehicles increased in 2015, partly because these vehicles had more safety content and telematics.

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Fleet operators and lending institutions have become more comfortable selling clean-titled vehicles in salvage auctions.

## SALVAGE AUCTIONS: AN IMPORTANT SOURCE OF DIVERSE INVENTORY

In 2015, the overall salvage marketplace experienced an increase in volume and moderate downward price pressure while overall demand remained strong. There were two distinct segments of the salvage market with divergent pricing trends: total-loss vehicles and those with lighter damage. Total-loss vehicles experienced strong downward price pressure from a decrease in scrap metal prices. This was led by the continued softening Chinese manufacturing sector and the price of oil dropping below \$30 per barrel. In recent years, two large consumers of scrap metal have been the U.S. oil fracking industry and the Chinese manufacturing sector. Both segments experienced a slowdown from 2014, and this caused the price of scrap metal to drop further, making it tough on sellers to dispose of vehicles in the lowest tier of the salvage market. On the other end of the salvage spectrum, vehicles with light to moderate damage experienced a slight decrease in year-over-year price drop as the supply increased but available buying market held steady.

Both trends should continue in 2016 as the available supply of salvage vehicles will steadily increase. Strong used vehicle demand will ease the slight downward price pressure on light to moderately damaged salvage vehicles, while the lower price tier vehicles will stay at historically low values as scrap metal prices remain low. In particular, the growing size of vehicles in operation in the U.S. plays a part in the salvage market. The number of vehicles in operation in the U.S. continued to grow, powered by strong new vehicle sales and a moderate rate of vehicles going to scrap. The average age of vehicles on the road is over 11.5 years old, a number held in check by strong new vehicle sales versus the number of vehicles scrapped. Two contributing factors to this trend continue to be higher-quality vehicles and a growing segment of the auto-owning population unwilling or unable to replace their older vehicles (9 years and older) due to a weak economic position. In fact, there were nearly 5 million more new vehicles sold than vehicles scrapped in 2015.

### ACTUAL CASH VALUES

Actual cash values (ACV) for total-loss vehicles increased in 2015. The increase in ACV is partly from vehicles' having more safety content (increase in airbags) and telematics, which increase overall vehicle value. This trend will continue in 2016, staying in line with increasing average new vehicle sales transaction prices.

### SALVAGE AUCTIONS REMARKET MORE CLEAN-TITLED VEHICLES

Fleet operators and lending institutions have become more comfortable selling clean-titled vehicles in salvage auctions when the vehicles have excessive miles, wear and tear, or age. This remarketing channel offers a

Salvage auctions remain one of the most variable marketplaces within automotive remarketing. These sales market many different products, from recovered theft inventory to late model rental units, to vehicles with catastrophic loss.

wider spectrum of buyers for these vehicles. On the buying side of the transaction, while dealers continue to focus primarily on clean-titled vehicles, they have become increasingly comfortable purchasing salvage-titled units. Units will typically receive a salvage title when the cost of repairs exceeds 75 percent of the vehicle's actual cash value, but there are notable exceptions. Units that are stolen or are excessively older with higher mileage could receive a salvage-title brand. Near-term historical demand has made these units more attractive to the wholesale buyer than they would have been otherwise.

### DEALER PARTICIPATION INCREASES IN SALVAGE AUCTIONS

Salvage sales are increasingly co-located within traditional auction sites, allowing buyers to gain additional exposure to and familiarity with these vehicles. Independent dealers in particular have found salvage units to be a profitable source of inventory. While off-lease volumes will become more plentiful to independent buyers in coming years, the salvage segment will retain much of the favor it has garnered. As dealers recognize that these units can be repaired and sold to retail buyers, bidding activity increases, including activity from digital sales channels such as Simulcast.

### INTERNATIONAL BUYERS COMPETE FOR LATE-MODEL REPAIRABLE UNITS

The trend of international buyers' sourcing inventory from salvage auctions faced some headwinds in 2015, driven primarily by currency fluctuations, changes in the auto import process for vehicles bound for Mexico, and softening economies in key international markets. Still, international buyers played a key role in the salvage segment as digital platforms connected buyers to desired inventory across great distances. Indeed, Manheim reported that it shipped vehicles to more than 170 countries. Mexican importers continue to favor more affordable nonluxury units and often compete with domestic buyers, leading to increased bidding activity. Buyers from the Middle East and Europe continue to favor late model vehicles, particularly those from luxury manufacturers. The demand from China slowed down in 2015, reflecting a continued cooling-off of the Chinese economy.

## AVERAGE VEHICLE TOTAL LOSS ACTUAL CASH VALUE

Vehicles	Q1/13	Q3/13	Q1/14	Q3/14	Q1/15	Q3/15
	Average Actual Cash Value					
<b>Convertible</b>	9,965.07	10,350.22	9,629.03	10,146.85	9,507.76	10,130.35
<b>Coupe</b>	7,160.85	7,456.84	7,152.97	7,533.04	7,497.37	7,868.84
<b>Hatchback</b>	7,899.19	8,253.50	7,962.19	8,458.86	8,208.48	8,720.10
<b>Sedan</b>	7,201.49	7,459.44	7,209.71	7,721.12	7,426.76	7,889.38
<b>Wagon</b>	7,507.11	7,401.85	6,961.64	7,046.74	6,623.72	6,740.59
<b>Other Passenger</b>	15,186.71	13,938.03	16,668.16	13,722.77	16,196.74	14,644.66
<b>Pickup</b>	9,691.98	9,850.29	10,105.82	10,428.99	10,868.37	11,049.70
<b>Van</b>	5,784.86	5,873.80	5,676.85	6,123.50	5,994.83	6,377.62
<b>SUV</b>	9,051.49	9,411.71	8,847.89	9,544.26	9,301.24	10,020.46

Source: Mitchell Industry Trends

### SALVAGE BUYERS RELY ON TECHNOLOGY

As in the whole-car business, salvage buyers have become increasingly dependent on technology to buy, sell, and manage their inventory. Multiple purchasing options exist, including real-time sequential bidding via Simulcast, 24/7 bidding and buy-now sales via OVE.com, and new mobile bidding technology allowing buyers to place live bids from Simulcast sales via a mobile device. Buyers often attend physical sales and purchase their vehicles at one location, while purchasing vehicles from a second location using their mobile devices. Online tools present the buyers with information, timely market trends, and greater access to inventory. Sellers benefit from the dynamic of an expanded buyer base ready to do business.

### 2015 BRINGS INCREASED VOLUME AND PRICE DECLINES WITH FALLING COMMODITY PRICES

Salvage auctions remain one of the most variable marketplaces within automotive remarketing. These sales remarket many different products, from recovered-theft inventory to late model rental units, to vehicles with catastrophic loss. The salvage market experienced strong demand but downward price pressure with commodity prices coming down from market highs. In 2015, volume at Manheim auctions for salvage units increased by more than 27,000 vehicles sold versus the prior year. The average price of the salvage vehicles experienced a moderate decrease from 2014, with pressure coming from lower commodity prices. Not unlike in previous years, values are affected by the ultimate disposition of the unit. Some buyers intend to

part-out the vehicle and sell the remaining recyclable components for scrap, while others will invest in repairs and will ultimately resell the unit to retail buyers.

Global commodity prices will always heavily influence this industry segment, and 2015 was no different. Key commodity prices for aluminum, platinum, and palladium decreased in 2015 and impacted the scrap market. Over the past 24 months, the scrap metal marketplace has shown a steady decline that picked up the pace of decline in 2015; the overall values of crushed auto bodies decreased nearly 50 percent when comparing 2015 to 2014.

Foreign demand from China, Turkey, South Korea, Taiwan, and Japan was softer throughout 2015. Similar to 2014, foreign exports affected values by introducing more low-priced steel into the marketplace, depressing prices for scrap steel and crushed auto bodies alike.

Noninsurance vehicles experienced two distinct trends in 2015. Newer, lightly damaged vehicles continued their run of strong demand, bought by dealers and exporters alike, as the price trends mirrored those of the whole-car auctions. Noninsurance end-of-life vehicles experienced significant price declines, driven by the falling scrap metal market.

**2016 USED CAR MARKET REPORT**

# **INTERNATIONAL**

## 2015 HIGHLIGHTS

Global passenger car sales were expected to reach a new high of 89.4 million units in 2015.

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China retained its position as the largest auto market in the world (though the rate of growth has slowed), with the U.S. and Japan following behind.

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In the U.K., new car sales reached a 10-year high (2.47 million), while used car sales reached a six-year high of 7.2 million units.

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New car sales in Australia reached a record 1.16 million, while new car affordability reached a 40-year high due to wage increases and low interest rates.

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While used car sales in India only equaled new car sales in 2014, they are expected to triple in size by 2019, surpassing new cars substantially.

**GLOBAL**

At the end of 2014, global sales of new passenger cars grew 4.6 percent to reach almost 70 million units, while total vehicle sales grew to over 88 million units. In 2015, passenger car sales were 89.4 million, which is the sixth consecutive record result.

China retained its position as the largest auto market in the world even though the rate of growth has slowed. Elsewhere in the major markets, early results suggest the USA and Japan retained their 2nd and 3rd place positions, respectively, in global new vehicle sales. However, Brazil dropped to 7th place behind Germany, India, and the UK; and France and Canada overtook Russia.

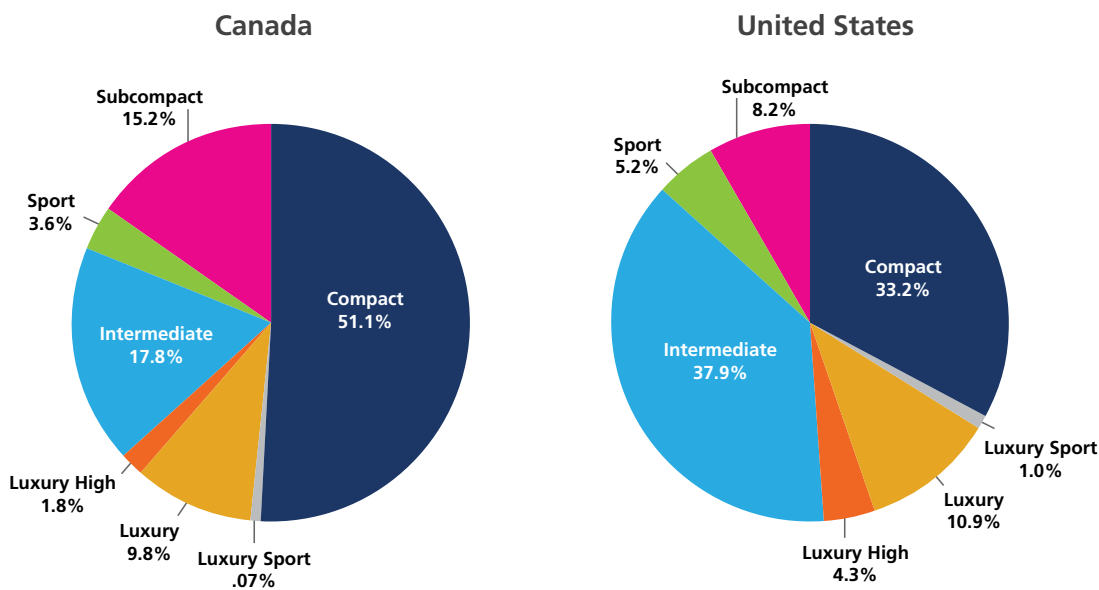
**CANADA**

Ownership of vehicles—both new and used—grew to record levels in 2015, a positive for used vehicle sales since consumers’ first vehicle is usually used. Used vehicle sales will continue to grow in importance in 2016 as new car dealers make the used side of their business a bigger focus, a development in part spurred by affordability concerns on the new car side. This has been one of the major differentiators between the Canadian and U.S. markets in the past, as Canadian new car dealers have not prioritized their used car operations nearly as much as U.S. dealers. Used car supply will continue to increase in years ahead in part due to increased lease returns—with originations returning to the 20 percent-plus level over the last few years (still far short of the 50 percent level achieved before the financial crisis).

Cox Automotive Canada was formed in May, 2015. Over the course of the year, the company established a marketing awareness campaign for Cox Automotive Canada and all its brands and launched a dedicated website ([www.coxautoinc.ca](http://www.coxautoinc.ca)). Manheim Canada expanded its footprint into Western Canada in 2015 with the addition of Manheim Vancouver and acquisition of Manheim Edmonton in order to serve clients in these markets. Today, there are a total of five auction locations in Canada.

Cox Automotive also formed a partnership with Canadian company XLane, launching the Digital Showroom and Instant Auction platforms. This partnership supports the company’s digital auction strategy and provides clients additional options to buy and sell vehicles.

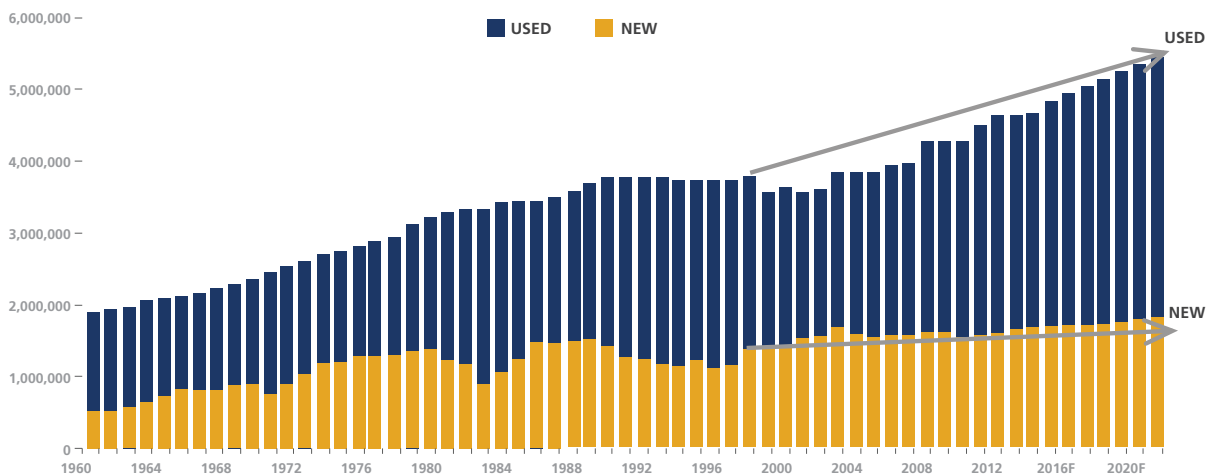
2014 LIGHT VEHICLE SALES MARKET SHARE BY PASSENGER CAR SEGMENT



Source: DesRosiers Automotive Consultants Inc., GAC, CVMA and Ward’s Automotive Reports



## NEW VS. USED VEHICLE SALES IN CANADA 1960-2020F



Source: DesRosiers Automotive Consultants Inc.

Other trends to watch in Canada include: continuing increases in the export of used vehicles to the United States, stable resale values as a result of an increase in used vehicle supply, and the growth of subprime lending in the used vehicle marketplace. Further, as used car sales continue to grow in volume and importance to dealer profitability, segmentation in terms of vehicle age continues to gain importance as a differentiator in determining vehicle value.

### U.K. MARKET

New car sales in the UK reached a 10-year high in 2014 of 2.47 million registrations, a 9 percent increase over 2013. Growth rates were expected to slow in 2015, but the market continued to break records. December was a record month (up 8.4 percent compared to December 2014), and marked 46 months of consecutive growth. Year-end results showed an all-time record of 2.63 million sales, up 6.3 percent on prior year.

The used car market reached a six-year high at 7.2 million units in 2014, an increase of 5.8 percent on the 2013 sales of 6.8 million. The average age of these used cars was just below 8 years old—a recession legacy following the dive in new car sales that resulted in a shortage of younger cars in the market today. Used car sales have still not yet recovered to the pre-recession high of 7.7 million in 2004, but recovered significantly since the fall to 6.7 million in 2012.

In the wholesale market, over 1.5 million vehicles are sold through the National Association of Motor Auctions (NAMA), of which Manheim is an active member. Car sales through NAMA members are 4 percent up on 2014 levels, and sales of vans and heavy trucks are up by 12 percent. 2015 total used car sales are expected to be 3 percent ahead of 2014 levels.

Manheim is the No. 2 auction company in the United Kingdom, with 17 auction centers nationwide, and a number of online auction and fixed-price buying channels, including Dealer Auction—a trade-only online auction offering trade-ins exclusively from franchised dealers.

Movex is a recent addition to the Manheim U.K. portfolio. Movex is a vehicle logistics platform which, akin to Ready Logistics, is designed to maximize efficiencies on auto movements by connecting transport providers and the automotive trade.

Cox Automotive consumer brands in the U.K. include motors.co.uk—the U.K.'s second-largest online classified, and consumer car-buying brands of WeWantAnyCar.com and money4your-motors.com. In addition, Retail Services provides software solutions to manufacturers and dealer groups across the U.K., including websites, used stock locators, dealer stock management systems and after-sales solutions.

Both new and used car sales were largely driven by favorable market conditions—interest rates are still at a record low (the Bank of England base rate has been 0.5 percent since 2009), consumer confidence is high, fuel prices are low, there is an abundance of finance options, and the uncertainty around the May 2015 general election did not seem to have had any impact on market confidence and sales.

Approximately three-fourths of consumer new car sales are financed, and Personal Contract Plans (PCP) deals drive this. PCP allows drivers to pay an initial deposit and then a fixed monthly payment over an agreed term based on an agreed annual mileage (allowing for depreciation). At the end of the term, the driver can either pay the balloon payment to take full ownership of the car, or trade it as a deposit for a new car. Recent reports suggest the market may be subject to increased mileage fraud as consumers try to avoid any penalties for exceeding agreed mileages.

Manheim U.K. undertook primary research of dealers where findings suggested the majority of dealers expect that the car will be traded in at the end of the term. In turn, Manheim expects to see a high volume of PCP returns into the auction market from 2017 onward.

Used car prices continued to rise in 2015, and there are fears that this cannot continue if OEMs continue to 'force' new car sales and more used vehicles appear in the market following the recovery from recession.

## CONTINENTAL EUROPE AND TURKEY

The global financial crisis impacted Europe heavily, and the road to recovery is taking place at varying speeds across the markets.

Italy's economic growth stagnated at the end of 2014, Spain saw its strongest growth in a quarter during Q2 2015 of 1 percent—which is the highest since 2007, and Portugal is still recovering from strict austerity measures following international financial 'bailouts' in the wake of the crisis.

Other factors impacting recovery across the region as a whole include the ongoing Russia/Ukraine crisis and economic sanctions, the situation in Syria, and the threat of Greek withdrawal from the E.U.

New car sales in 2015 showed a 9.3 percent increase from 2014 to 13.7 million units—the best result in five years—with double-digit growth results for Spain (+20.9 percent) and Italy (+15.8 percent). December marked 28 consecutive months of growth across the region, which is positive although sales have not reached pre-crisis results. Sales growth has been driven by OEM incentives, improved access to finance, and government scrappage schemes. However, these stimuli are not considered to be sustainable in the long term.

Manheim currently has physical and online auction presences in Portugal, Spain, Italy and Turkey—where it is a market leader. Mobile Simulcast units support sales in Italy, Spain and Turkey. In addition, Manheim has two car buying service businesses, which launched during 2014 in Portugal and Turkey—Venda Ja and Otomax respectively.

An additional Cox Automotive brand is German-based Modix, which supports car dealers and OEMs with their digital marketing challenges, including dealer websites, used vehicle locators and lead tracking systems. Modix is currently across 18 countries with over 6,000 dealer customers and 30 OEMs.

Spain, Portugal, and Italy all showed growth in new car sales in 2015. Italy had growth of 15.7 percent against 2014 to 1.58 million units, the best result in four years. Used car sales were reported at 2.5 million for 2014.

In Portugal, new car registrations had declined since 2005, but 2014 saw a 35 percent increase on prior year to 143,000 following the end of austerity measures in the market. The 2015 results show a 9.3 percent increase on prior year to 178,500.

Spain has shown consistently strong growth, with double-digit increases in 2014 and 2015, partly due to economic recovery but also a very popular government scrappage scheme. Year-end results for 2015 reached 1.03 million (21 percent increase on 2014). Spain used car sales were reported at approximately 1.7 million units in 2014.

The European car parc has aged during the recession—Portugal's average car is now 12 years old, up from 10.1 in 2010. Over a quarter of the Italian car parc is more than 15 years old, and Spain has an average car parc age of 11.5 years.

Although Turkey remained resilient despite the global financial crisis, political uncertainty, and an escalation of regional violence, it has seen business and consumer confidence drop to the lowest levels since 2009.

New and used car sales in Turkey were expected to decrease by 5 percent in 2014 due to changes in interest rates and exchange rates, increases in car taxes, bank credit restrictions, and a slowdown in private-sector investments. New car sales ultimately dropped by 12 percent in 2014 compared to 2013. Used passenger car sales dropped 10 percent from 4.2 million (2013) to 3.8 million in 2014.

Despite the uncertainty caused by the political elections during the last quarter, the year-end results for new car and LCV sales achieved a new record, falling just below the 1 million sales barrier. The average car age is 16 years in Turkey, while 25 percent of the 14 million vehicle parc is over 20 years old.

### ASIA PACIFIC

In the Thai market, new car sales reduced to pre-2012 levels, at around 900,000. This, however, could be considered 'normal' following the end of the government's 'first car buyer' financial incentive scheme, which increased new car sales during 2012 and 2013.

Used vehicle sales were estimated at around 1.8 million in 2014—falling from 2.1 million in 2013, which could be an impact of the government incentives around new car sales.

Australia is experiencing an economic slowdown following the end of the resources boom and a reduction in house price growth. The automotive production industry will cease in 2016/17 as Ford, Holden and Toyota—the last of the manufacturers—exit the market.

Although new car sales dropped by 2 percent in 2014 to 1.1 million, 2015 results showed a 3.8 percent increase to a record 1.16 million. New car affordability reached a 40-year high in June due to wage increases and low interest rates. The October election of a new government has seen stronger results in the business and consumer confidence measures.

Manheim has physical and online auction presence in Australia, New Zealand and Thailand. In addition, Australia also offers a consumer car buying service—sellmycar.com.au, and Dealer Auction—a trade-only online auction offering trade-ins exclusively from dealers.

The estimated size of the used car market in Australia was approximately 3.7 million units sold in 2014. Annual growth in used vehicle wholesaling has been 3.7 percent over the past five years, with the annual growth for 2014-19 expected to be 5.2 percent per annum.

Moving on to New Zealand, despite a slight acceleration during Q2, economic growth remained relatively weak, attributed to weaker results in the dairy, agriculture and mining sectors.

Although total new vehicle sales were flat in 2014 with 114,000 units sold, 2015 year-end results showed a record for total new vehicle sales, which were up 5.4 percent, reaching 134,000. The estimated size of the used vehicle market is 110,000 vehicles per annum, and the majority of these—99,000 in 2014—were imports, mostly from Japan.

### BRAZIL

Currently the seventh-largest economy in the world, early-year forecasts had suggested Brazil will move to fifth place by 2030. However, the economy fell into recession during 2015 with recent figures suggesting a 3 percent contraction. As a result, the government has introduced strict austerity measures to help recovery through reduced spend and subsidies, and increased tax.

Manheim entered Brazil, the fourth-largest car market in the world, in 2014 following an acquisition of an established auction site in São Paulo called CarBizz.

The recession has clearly impacted the new total vehicle market. Brazil had retained its 4th place position at the start of 2015 with new vehicle sales exceeding 3.5 million, however year-end results for 2015 showed a drop to 2.6 million. The 2015 results from the largest markets suggest Brazil may have fallen to 7th place behind India, Germany and the UK.

Used car registrations were suggested to be around 9.6 million units (2013) with a new to used car ratio of 1:3. This market was forecast to grow by 7.5 percent CAGR by 2018; however, this growth rate was set pre-recession.

### CHINA

China has been the largest auto market in the world for seven consecutive years, with sales of 23.5 million new vehicles in 2014. At time of print, the 2015 total new vehicle sales results had not been issued; however, the forecasts suggested a 7 percent increase to 26 million

vehicles. The new car sales result for 2015 has been announced at 21.1 million sales. To put into context, this result was larger than sales across the whole of Europe. Government tax incentives to stimulate new car sales growth were introduced in September and focused on low-emission vehicles. This will continue into 2016.

Used car sales were estimated around 6 million (1 million more than 2013), which demonstrates how 'immature' the market is. By 2017, this is expected to reach 9 million. The current vehicle parc of 127 million is estimated to include 101 million cars alone.

Cox Automotive has investments in three businesses in China: BitAuto provides digital marketing, websites and CRM solutions, as well as the leading automotive classified Taoche.com; Autostreets.com is an e-commerce platform that includes physical and online auctions; and Jingzhengu, another joint venture to provide used car valuations for dealers and consumers, is backed by Kelley Blue Book.

The 2015 rate of economic growth was the slowest in 25 years at 6.9 percent, attributed to the shift in focus from exports and investment to consumption. In August, the stock market crashed in what was dubbed 'Black Monday.' Interest rates reduced and the currency devalued, resulting in concerns around a potential knock-on effect to the global economy.

## INDIA

India is now the 5th largest market in terms of new car sales (overtaken by Germany in 2015), with 2.78 million units sold.

While the size of the used car market only equalled the new car market in 2014, it is expected to continue to triple in size by 2019, surpassing new car sales substantially.

Although two-wheelers dominate almost 80 percent of the market, there are approximately 19 million cars on the road in the country. However, the motorization rate is very low, with just 20 cars per 1,000 people, offering a large potential for growth.

With India's growing new vehicle market leading to accelerated growth in used car sales, in November of 2015 Cox Automotive announced an investment in Mahindra First Choice Wheels Lmtd., India's largest multi-brand certified used car company. MFCWL has more than 650 franchised outlets in nearly 300 locations in India. Other operations of the business include Indian Blue Book (India's only used car pricing guide), the auction platform eDiig, and AutoInspect, its third-party inspection business. The Indian used car market is expected to grow from 3.6 million units sold in 2014 to 9.6 million units by 2019.

## STATE OF THE EXPORT MARKET

With U.S. new car sales expanding in 2013 and 2014, the used car remarketing pipeline in 2015 and beyond will see a significant spike in U.S. used car exports globally. Demand is also on the rise as economies in developing countries begin to strengthen.

In addition to supply and demand, certain countries that rely heavily on the U.S. export market are also relaxing their import requirements, further enabling the supply chain. The North American Free Trade Agreement (NAFTA), which currently restricts the age limit of cars imported into Mexico to 6 years of age and older, will relax the age requirement by two years every year until 2018, when the age restriction will be completely lifted and all cars may be imported. China has also announced that it will relax some of its used car import requirements, but details have not yet been released. Similarly, countries across Africa are also relaxing import requirements, further enabling the fastest-growing U.S. export market.

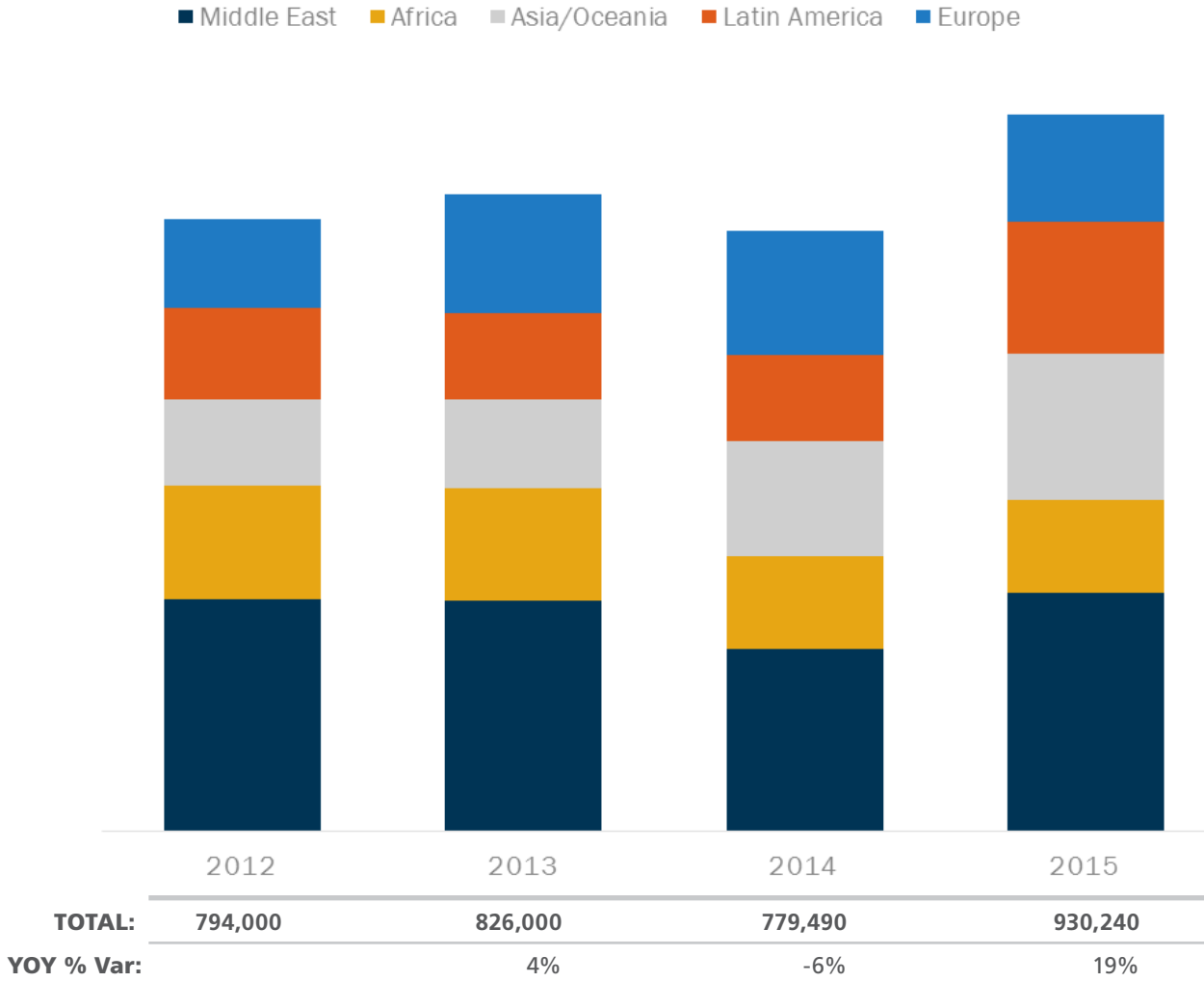
While the U.S. used car export market has been traditionally dominated by a large number of smaller dealers, there has been a paradigm shift in the supply chain, bringing much larger dealership groups and global companies into the used car export realm. Due to the financial resources and capabilities of these large competitors, their ability to quickly capture market share will create new opportunities globally.

The top five markets for U.S. used vehicle exports are:  
 United Arab Emirates, Saudi Arabia, Germany, China and Nigeria.

Along with all of the used car supply chain enablers comes a host of challenges. Many countries around the world are paying closer attention to the environment and making strides in becoming “greener.” As a result, increasing restrictions on import requirements, namely the sizes of engines and emissions, are limiting the supply chain. Many countries have placed higher tariffs on large-engine vehicles, making it more costly to import muscle cars and large SUVs while reducing, or in some cases eliminating, tariffs on hybrid vehicles, 4-cylinder, or 1.8-liter engines.

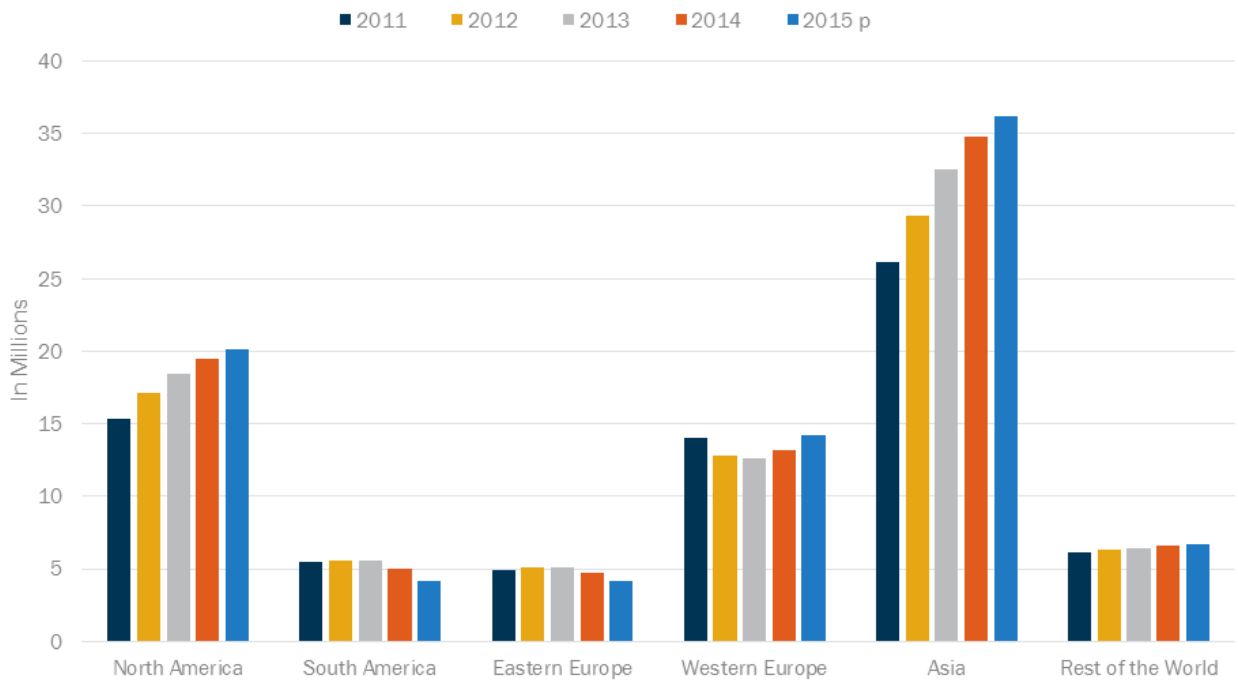
Another changing dynamic that is also enabling the export supply chain is the increasing confidence of the foreign-based buyer in the Internet. International dealers are relying more heavily on Web platforms to buy used cars from the U.S. and other markets globally. They are becoming much more comfortable and trusting online condition reports, car history reports, and grading of vehicles to make their purchasing decisions. What this also means is that accessibility to data, analytics, comparative pricing, and intelligence has also become prominent. Foreign-based dealers are just as resourceful and educated about all aspects of the supply chain as domestic-based exporters.

GROWTH VOLUMES IN EXPORT



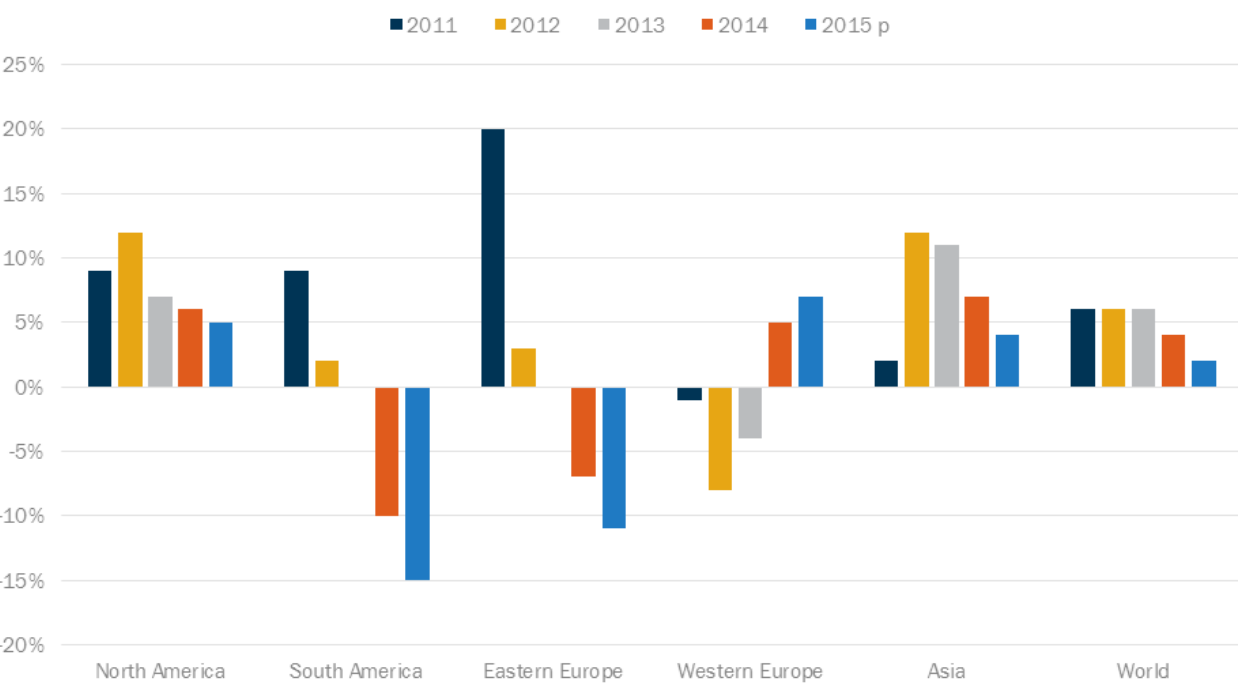
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NEW VEHICLE SALES BY REGION



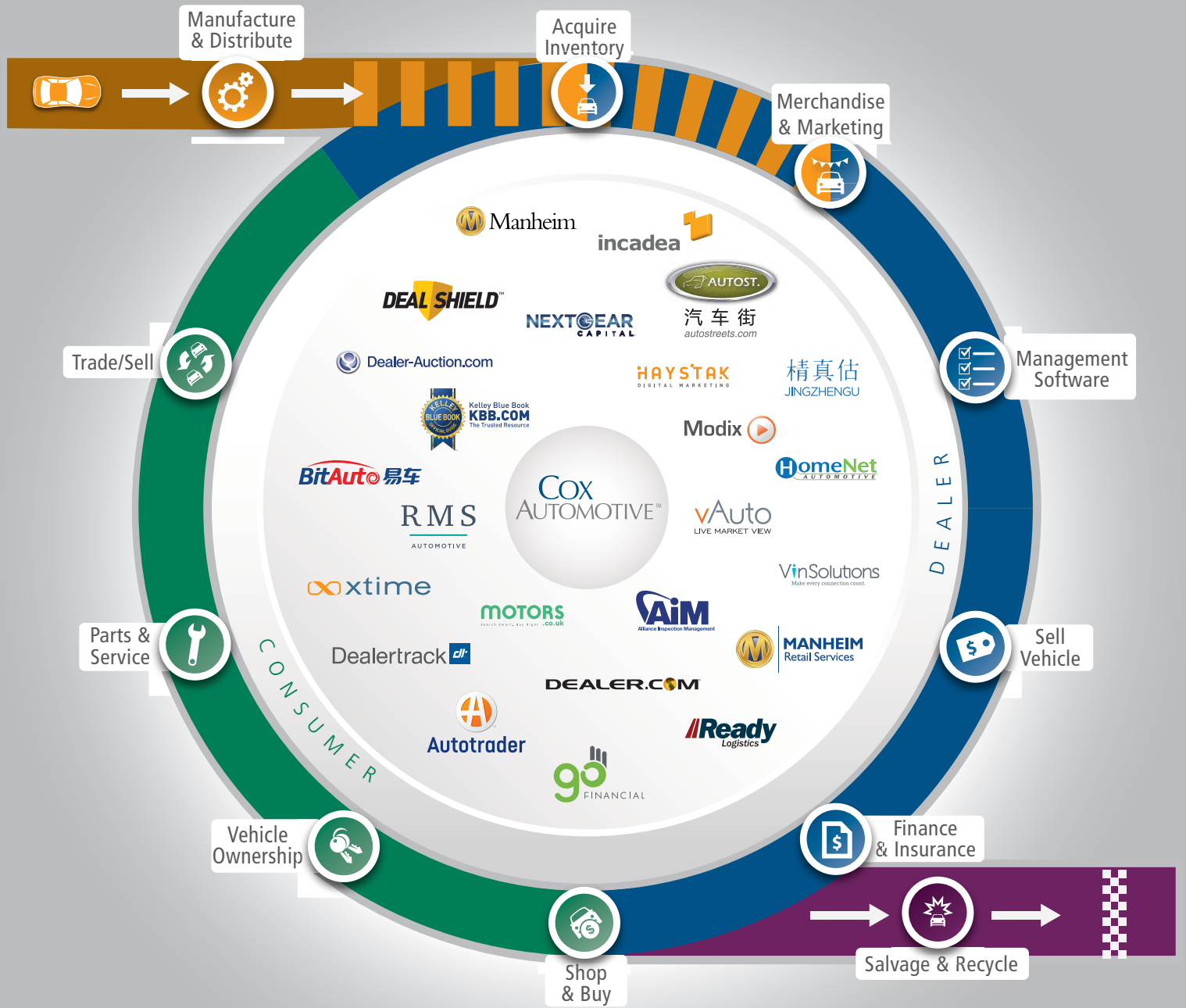
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YEAR-OVER-YEAR CHANGE IN NEW VEHICLE SALES



Compiled from multiple sources





## ABOUT COX AUTOMOTIVE

Cox Automotive is a leading provider of products and services that span the automotive ecosystem worldwide. Our goal is to simplify the trusted exchange of vehicles and maximize value for dealers, manufacturers and car shoppers. We've built the industry's strongest family of more than 25 brands to provide industry-leading digital marketing, software, financial, wholesale and e-commerce solutions to help our clients thrive in a rapidly changing automotive marketplace.

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