CREDIT UNION LEASING of AMERICA

CULA Study: Q2 2023 Credit Union Used Vehicle Loan Snap Shot

Credit Unions Worry About Over-Extension on Used Vehicle Loans, says New Survey, but Long-Term Loans Still Proliferate

Summary

Issues of affordability have driven consumers to focus on their monthly payment as a key priority when applying for a loan with the result that they are often opting for used vehicles with longer term loans. In fact, Experian's Q1 state of the automotive market report showed that 30% of used loans are 73 to 84 months or more (1% are over 85 months) and that loan delinquencies rose past pre-COVID levels in 2023.[1]

To find out how this is playing out in credit unions, CULA conducted a snapshot online survey of credit union professionals during the second quarter of 2023. The results not only revealed that over-extension on used vehicle loans is the number one concern for credit unions, but also the existence of a slight disconnect that is helping to generate that concern: credit unions continue to offer car buyers a significant percentage of longer-term loans, with low down payments, on high mileage older vehicles – and the majority are extending LTV by over 125%.

The results also indicate that used vehicle borrowers are evenly split on long- and short-term loans, probably due to high vehicle prices: consumers are either looking for the lower payments of a long-term loan or the lower commitment of a short-term loan.

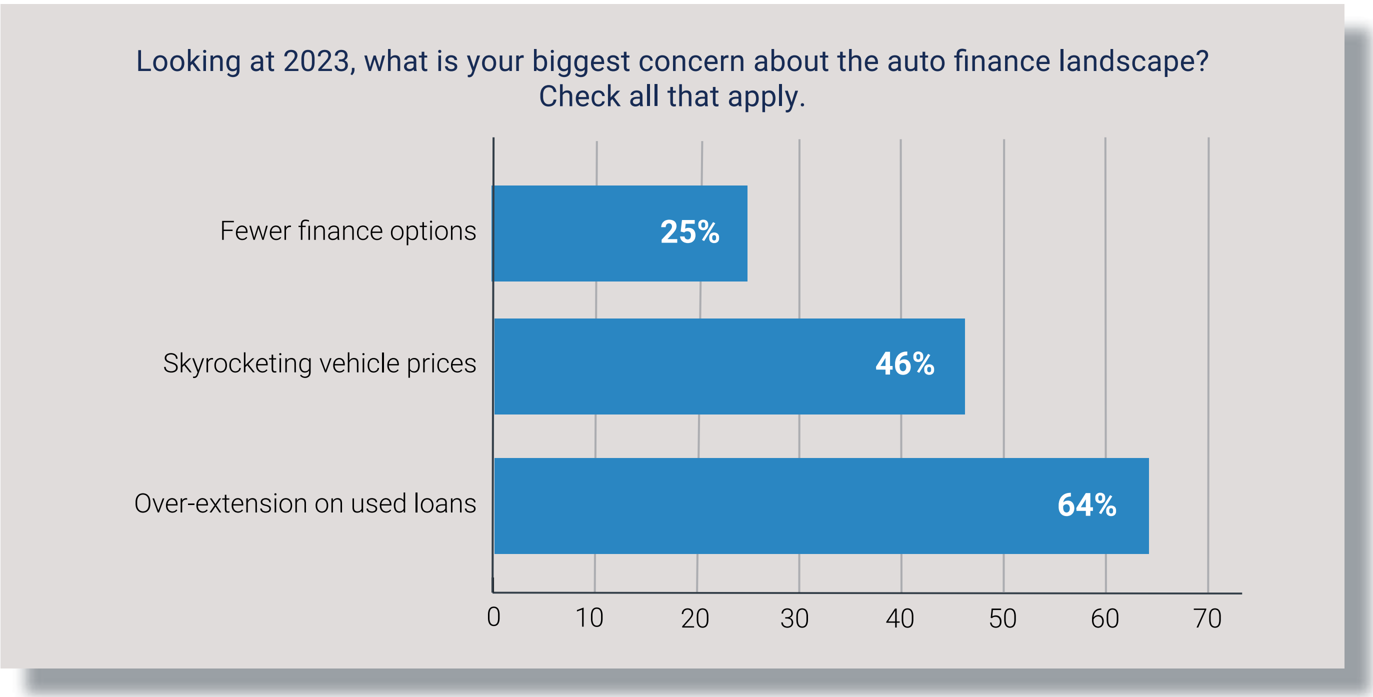
Overwhelmingly, credit unions say they want a better alternative to long term loans and agree that, in today's economy, the best answer would be short-term financing with affordable payments and higher yield.

[1] *https://www.experian.com/content/dam/noindex/na/us/automotive/finance-trends/2023/2023-q1-state-auto-finance-market.pdf*

Key Survey Results and Implications

Credit Unions are Worried About Used Vehicle Loans

Over-extension on used loans is by far the number one auto finance concern, with nearly two-thirds citing it as a big concern. Not surprisingly, nearly half of credit unions surveyed are also concerned about sky rocketing vehicle prices.

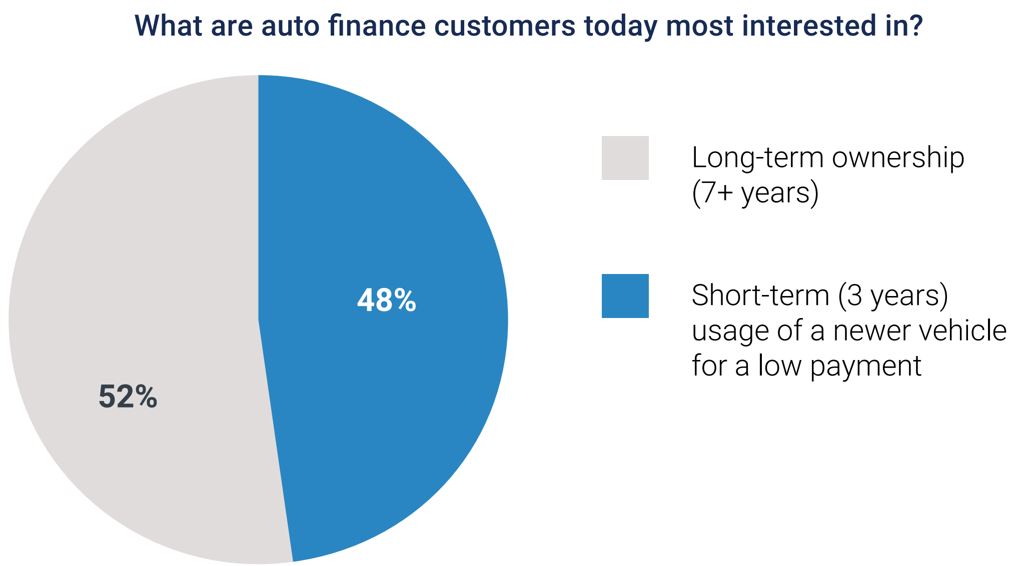


Even with a slight softening in prices, used vehicles still averaged an astonishing $28,381 in Q1 2023, a 44% increase from Q1 2018[2]. With many consumers paying such high prices for used vehicles compared to pre-pandemic prices, they are more vulnerable to finding themselves with negative equity, firmly upside down on their loans. And, as a result, in today's challenging financial environment often unable to get out of that loan. This means the risk of those borrowers walking away from that loan are greater. With consumers having paid too much and credit unions overextended, the end result is a bad situation for both lender and buyer.

[2] *The average transaction price is $28,381 a 44% increase from Q1 2018's $19,657. Current used values are much higher than they were before the pandemic regardless of the vehicle's age, make, model, features or mileage https://static.ed.edmunds-media.com/unversioned/img/car-news/analysis/2023-q1-used-vehicle-report.pdf*

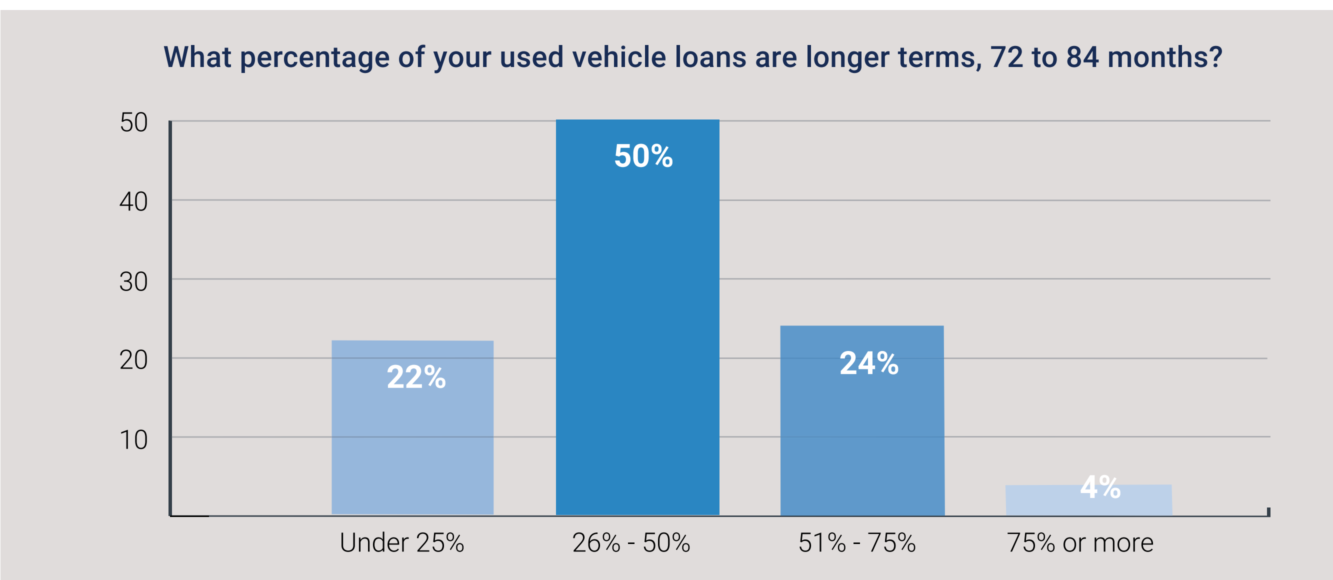
Consumers are Looking at Both Long-Term and Short-Term Loan Options

Auto finance customers today, say survey respondents, are almost evenly split in interest between long-term (52%) and short-term (48%) loans. This is probably a function of the vehicle affordability crisis and inflation: long-term loans are more desirable because the payments are lower, while short-term loans may be desirable because borrowers may want less commitment and to get into a lower grade vehicle until prices come down.



Long-Term Loans Popular at Credit Unions

At least one-in-four used vehicle loans are 72 to 84 months for the vast majority (78%) of credit union respondents. Nearly 30% of credit unions said that 51% or more of their used loans are longer term.

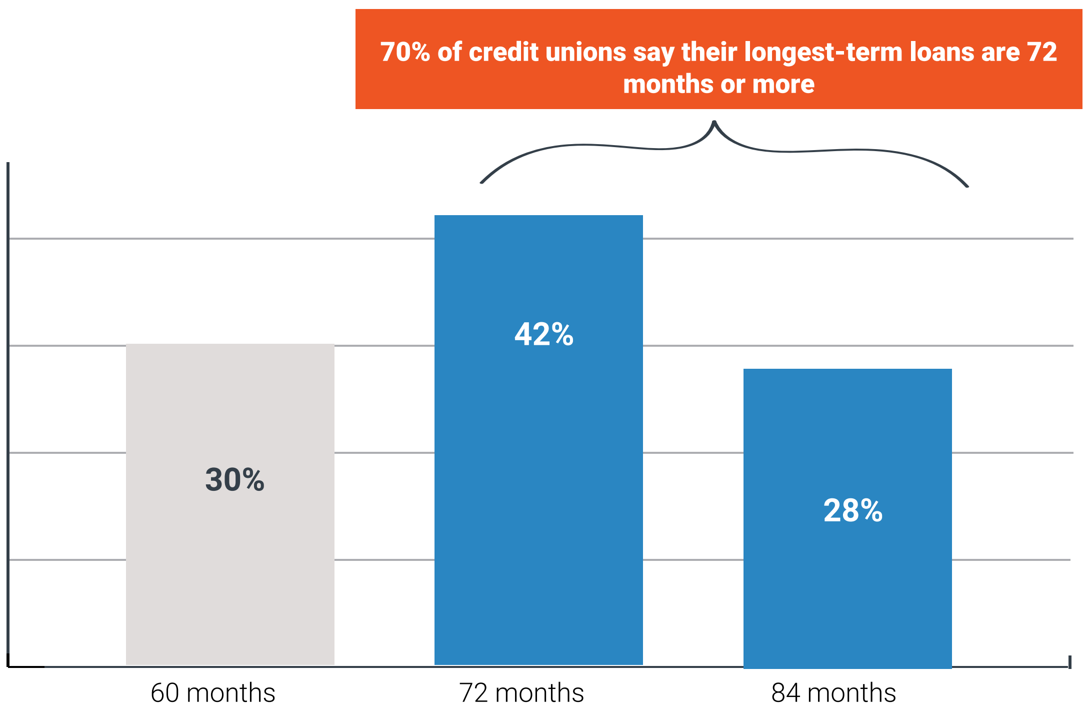


These results are not surprising given high used vehicle prices, indicating that consumers may not necessarily be thinking in terms of paying off their loans, but of getting to the lowest monthly payment possible. This adds to credit union worries about over-extension on these loans.

Majority of Credit Unions Offer 72-Month Terms or More

70% of credit union respondents say their longest-term loans are 72 months or more, with 28% saying that 84-month loans are their longest term.

What is your longest term on used vehicle loans?

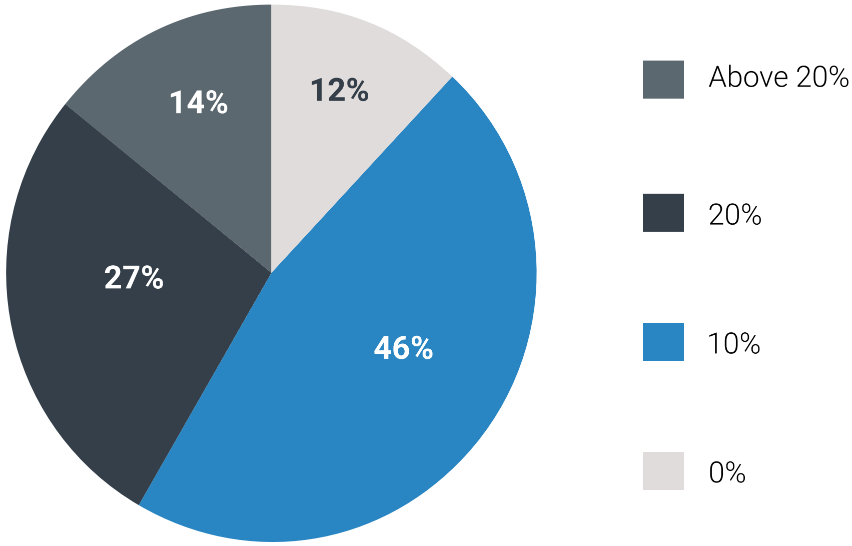


Of those credit unions reporting that 84 months are their longest-term loans, 55% say those make up one in five or more of their loans, with nearly a third saying that they make up over 40% of loans.

Majority Allow Low Down Payments, Intensifying Risk

The majority (58%) of credit union respondents require a 10% or less down payment on used vehicle loans. Only 14% ask for more than 20%. Loans with low down payments will likely be extended to the maximum and the borrower will be in negative equity for longer adding to credit union risk.

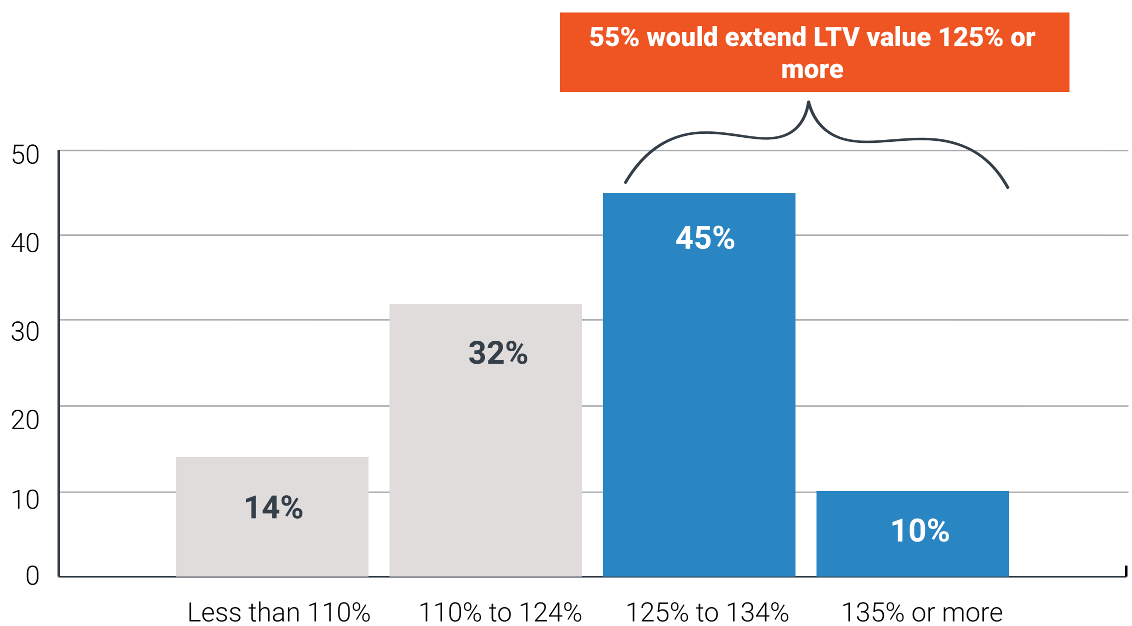
How much do you currently require as a down payment on used vehicle loans?



Majority Extend LTV Value 125% or More

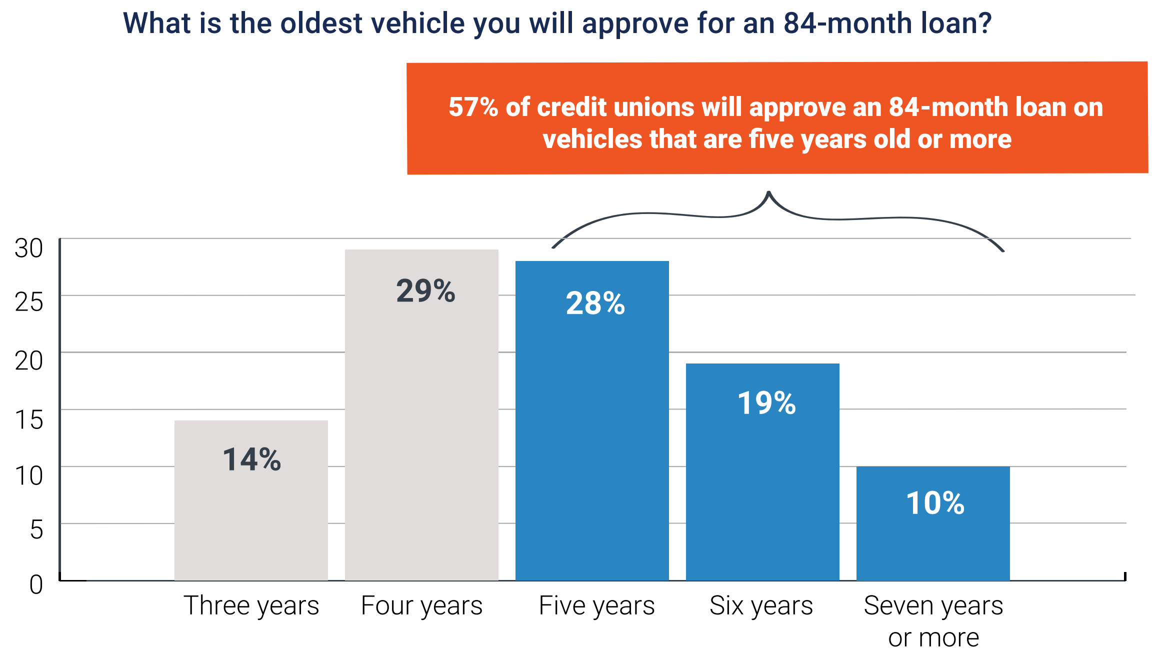
The majority (55%) of credit union respondents say they will extend LTV on used vehicle loans by 125% or more. While this may be beneficial for dealer partners – so they can offer warranties, LoJack, etc. – it means that a $40K car can quickly turn into a $50K loan, putting the consumer upside down and adding to credit union risk.

How far will you extend LTV (loan-to-value) on used vehicle loans?



Over Half Extend Loans on Older Vehicles

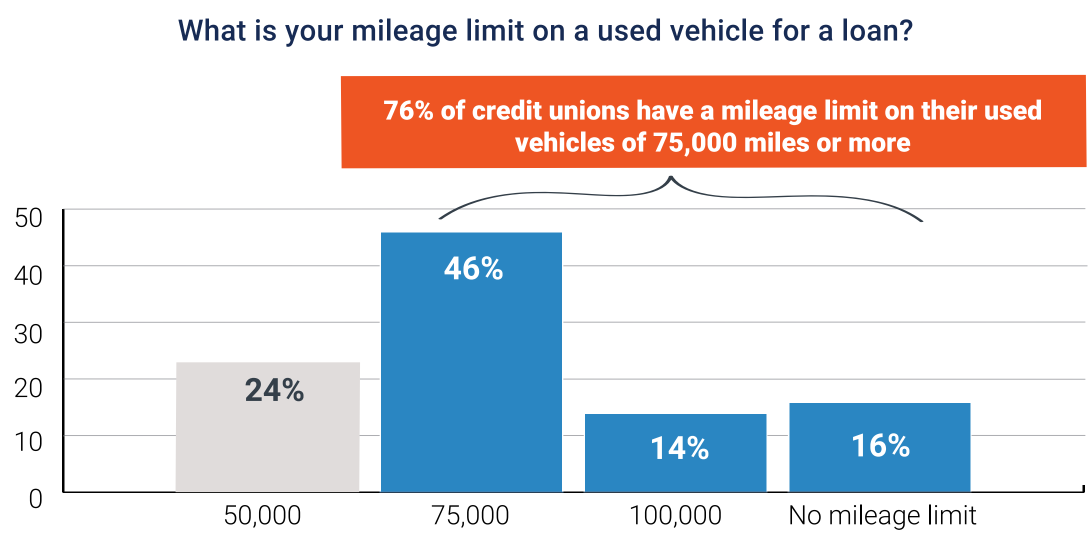
The majority (57%) of credit union respondents will approve an 84-month loan on vehicles that are five years old or more.



While today's vehicles are more dependable than ever before, adding seven years (or more) of ownership onto already older vehicles increases the likelihood the car will have reliability/repair issues, while the value dramatically decreases, creating risk for both borrower and credit union.

Most Credit Unions Allow 75K Miles or More

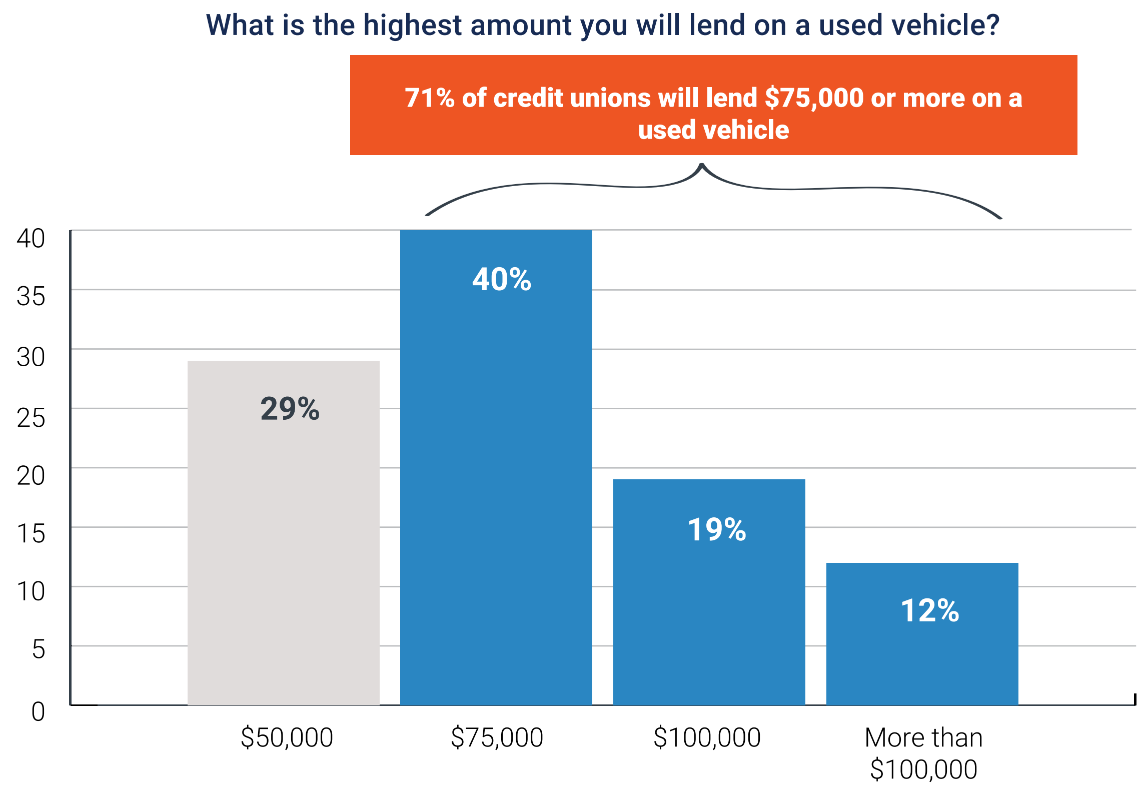
Nearly 80% of credit union respondents have a mileage limit on their used vehicles of 75,000 miles or more, with 30% extending that limit to 100,000 miles or more.



Extended mileage limits mean the likelihood of mechanical failure increases. Unless the credit union demands a warranty to make the loan, risk exposure increases.

In Spite of Risk, Vast Majority Will Lend $75K or More

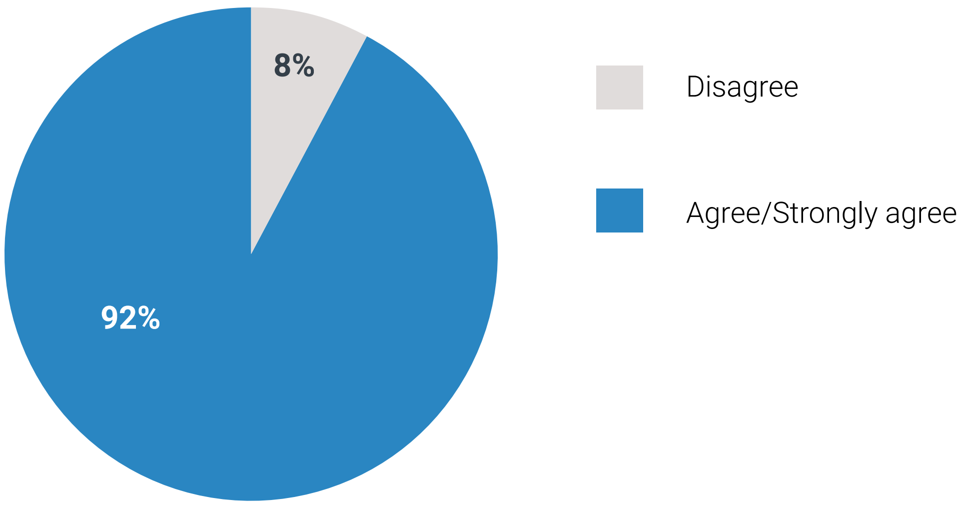
The majority (71%) of credit union respondents will lend $75,000 or more on a used vehicle, with nearly one-third (31%) saying they would lend $100,000 or more. It's a simple equation — the higher the vehicle price, the higher the risk to the credit union.



Conclusion

As these survey results make clear, credit unions will continue to incur unnecessary risk if they don't find an alternative to the long-term used auto loan, which they are continuing to offer in significant numbers – and on vehicles that present potential risk. In fact, the vast majority (over 90%) agree that they would like an alternative.

In today's economy, short-term financing with affordable payments and higher yield is a 'near-perfect' auto lending product.



Specifically, credit union respondents agree that short-term financing with affordable payments, that also offers credit unions higher yield, is the 'near perfect' auto lending product. Vehicle leasing, which checks all of these boxes, might just be the answer credit unions are seeking.

Methodology

Online survey conducted April 4th, 2023 through May 5th, 2023 among 415 credit union professionals.

About CULA

Credit Union Leasing of America (CULA) has been the leader in indirect vehicle leasing for credit unions for over 30 years. Founded in 1988, CULA provides best-in-class program assistance, analytics reporting, compliance support, dealer management tools and member services. The CULA indirect vehicle leasing program empowers credit union innovators to diversify their existing loan portfolios, improve yield and expand member services.

Visit https://www.cula.com/ to learn more.