



& Automotive Finance > Will Ai and Big Data create CHAOS again ?

IMPORTANT NEWS

6 May 2019

SITUATION: Banks and Financial Institutions seem poised to re-create the lending **Meltdown of 2008** via a renewed abuse of Asset Backed Securities (ABSs), this time in automotive finance.

"Total auto loan debt increased to \$1.23 trillion in Q1 2018, up from \$1.17 trillion versus a year ago. In Q1 2018, new auto loan originations totaled \$130.9 billion, \$39.8 billion of which was **subprime**. Annualized net loss (ANL) **rate** for subprime auto loan ABSs was 8.81%, up from 4.66% five years ago. Depreciation on used cars is accelerating and is expected to hit 17% in 2018, in contrast to 13% in 2017. " [Credit Chronometer].



WHY SIGNIFICANT: Securitization was designed for 'A' Credit. It relies on the Payment Streams from the loans and the Market Value of the underlying Asset, the vehicle. When the ANL doubles, the 'security' is weakened and may default. Worse yet, if the expected Market Value of the vehicle is less than expected / calculated, the default leaves a larger gap / loss. The gap might have been insured, but when the ANL doubles, the insurance can't cover the losses and collapses. This should sound familiar.

The technology tool that fed the 2008 subprime crisis was "computational finance", using **complex numerical algorithms** to 'bundle' the loans into saleable 'securities'. One problem was they used 'best case' in their calculations and left no margin for higher defaults and lower asset values. And all parties were sucking Fees out of the process, money which could have been reserved for Losses. They 'skated on thin ice' and crashed through.

- (1) the ABS numbers are so large and the trends are not good, possibly heading for a 'perfect storm' and another financial sector collapse.
- (2) the Tech giants muscling into banking will bring **Ai and Machine Learning** which could be like putting the ABS problem on steroids.

WHAT TO DO ABOUT IT: keep it simple; stop securitizing Sub-prime Credit. Set aside bigger Loss Reserves. The mathematics of the securitization process amplifies losses. We may be too late.

AI & Automotive is edited by Charles M. Parker, CEO Automotive Digest / Automotive Information Network.

Automotive & Ai developments are recognized and aggregated by Michael Pochan, Lecturer, CEO, Software Engineer, Marketing Strategist, and professional educator with Carnegie Mellon credentials and industry street cred. Mike was co-founder of LeaseTek, an application software company which was in 22 countries and had offices in Pittsburgh, London, Stockholm and Sydney. Some of their industry customers were Toyota Motor Finance Ltd. Ford Credit Europe plc, BMW Financial Services USA, VW Credit Canada, Hyundai Motor Finance, Volvo Finans A/S and Porsche Credit..

Send responses, rebuttals, & reaction to mpochan@edgsys.com or just yell loudly out your window.

###