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Watchdog Article: UPDATED! New GM's turn to subprime loans could prevent bailout payback

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Revelations that the New General Motors is using increased subprime lending to power its recent sales may doom any chance that taxpayers will ever recover the still-unpaid chunk of the $49.5 billion the federal government spent in 2009 bailing out the former auto industry giant.

The GM bailout came as part of the bankruptcy reorganization imposed by the Treasury Department's auto recovery task force formed in 2009 by President Obama shortly after his election to the White House. The reorganization was intended to help GM get through the deep sales slump it suffered in the Great Recession of 2008.

At the same time, Obama put the Treasury Department behind the acquisition of Chrysler Corp. by the Italian industrial giant, Fiat. Ford Motor Co., the original member of Detroit's once-almighty Big Three automakers, did not require government assistance because it had accumulated sufficient cash reserves to weather the recession.

As part of the reorganization, the New GM said it would repay the bailout loans, so government and stock market analysts alike are closely following the company's continuing problems in the market place.

Auto buyers with credit scores below 660 are generally considered to be subprime customers, but beginning in the fourth quarter of 2010 after the New GM acquired a loan company, AmeriCredit, that specializes in the subprime lending market. Since then, GM has gone in big on loans to customers with poor credit ratings, according to documents obtained last week by Investor's Business Daily (IBD).

"GM Financial auto loans to customers with FICO scores below 660 rose from 87% of total loans in Q4 2010 to 93% in Q1 2012," IBD's David Hogberg reported Friday.

"The worse the FICO score, the bigger the increase. From Q4 2010 to Q1 2012, GM Financial loans to customers with the worst FICO scores -- below 540 -- shot up 79% to more than $2.3 billion. The second worst category, 540-599, rose 28% from about $3.4 billion to $4.3 billion," Hogberg said. "Prime loans, those above 660, dropped 42% to $676 million." Go here for more from Hogberg.

Most GM car loans are financed through the company's Ally Financial, which was formerly known as the General Motors Acceptance Corporation (GMAC). But the presence on the balance sheet of a rapidly growing segment of car loans that are less likely to be paid could jeopardize the New GM's prospects for ever getting its stock price above $50.

That threshold is crucial because the U.S. Treasury still owns about 500 million shares of the New GM, or about 26 percent of the total. A November 2011 sale netted Treasury $23 billion, leaving the taxpayers still holding the bag for nearly $27 billion. The New GM stock is trading under $20 per share this week. The government estimated in May that it would lose about $15 billion were it to fire sale its New GM shares then when it was trading at $24 per share.

"GM is trying to expand the market by making high-risk consumers part of their customer base," said Dan Ikensen of the Cato Institute, a libertarian-oriented Washington think tank. "That may pump sales in the short run, but a significantly higher portion of GM's account receivables will have to be written off as bad debt, reducing the company's stock value going forward."

Ikensen is director of Cato's Herbert A. Stiefel Center for Trade Policy Studies.

"The U.S. treasury needs to sell its remaining 500 million shares of GM stock at an average price of $54 in order to make the taxpayers whole. The stock price, as of yesterday's close, was $19.71. Barring a natural disaster that affects all but GM's production facilities, GM's stock value isn't going to approach $54 within any foreseeable time horizon. Anticipated write-offs for bad debt, industry overcapacity, global economic stagnation, and the fact that the market knows that the U.S. government wants to dump 500 million shares as soon as possiblee all weigh negatively on the stock value," he said.

The turn to subprime loans "reflects a degree of desperation," said Prof. Todd Zywicki of George Mason University's School of Law. "This would be consistent with what a company might do if they have some confident that the government will bail them out. A prudent company certainly wouldn't do this kind of thing."

New GM signs $600 million European soccer sponsorship:

New GM sales are down here in the U.S. and in Europe, but that isn't prevening the bailed-out Detroit automaker from signing onto to a deal with a storied professional soccer team rated by Forbes Magazine as the world's most valuable franchise, according to Washington Free Beacon's Bill McMorris.

"GM's Chevrolet logo will appear front and center on the jerseys of soccer powerhouse Manchester United, as part of one of the largest sponsorship deals in U.S. history. GM will pay $60 million per year for the logo--nearly double the $31 million European insurance company Aon paid--despite plummeting sales and massive liabilities," McMorris reports this morning.

"The U.S. Treasury owns 26.5 percent of the stock of the Detroit-based automaker, which has been reeling from a dwindling European car market," McMorris said.

New GM's domestic sales are down this month 6.4 percent, year-over-year, the firm announced earlier this week.

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