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Watchdog Article: New GM's turn to subprime loans may mean taxpayers will never be repaid

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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-mighty 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 Ikenson 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."

Ikenson 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," Ikenson said.

"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 confidence that the government will bail them out. A prudent company certainly wouldn't do this kind of thing."

Zywicki, who is editor of the Supreme Court Economic Review, specializes in bankruptcy law, as well as consumer lending, credit and protection issues.

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