

*Accelerate Your Business*ECONOMY: MOVING AHEAD AT
MODERATE SPEED *page 1*RETAIL AND WHOLESALE
VEHICLE MARKETS *page 2*Q&A WITH TOM WEBB *page 5*

The **Auto Industry Brief** is published monthly by Manheim Consulting.

About Manheim Consulting.

Manheim Consulting is a business arm of Manheim, the world's leading provider of used vehicle services. Manheim Consulting comprises a team of automotive strategic consultants who work with clients to solve business challenges. With access to the most comprehensive used vehicle database in the industry, Manheim Consulting creates highly customized solutions for its customers to help them achieve greater success.

Manheim Consulting is dedicated to helping its customers drive business results and maximize their profit potential through a broad scope of services, including custom analytics, business optimization, macroeconomic analysis, data services, strategic development, research and more.

For more information, visit www.manheim.com/consulting or call 800-777-2053.

Annual Subscription: \$495

MANHEIM CONSULTING
6205 Peachtree Dunwoody Rd.
Atlanta, GA 30328

678-645-2377
800-777-2053

www.manheim.com/consulting

© 2013 Manheim Inc. All rights reserved.

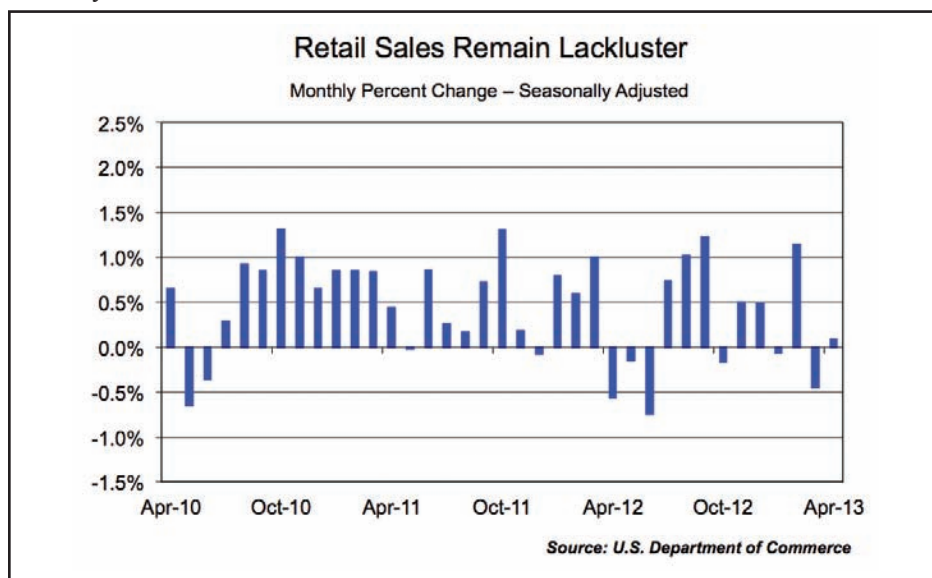
**SUMMARY**

The near term outlook for the economy appears to be clear sailing, but don't interpret that too optimistically – it will be “sailing,” not motor boating. In fact, a better expression would probably be “smooth rowing” since many business sectors will have to keep on working – and with some degree of synchronization – to keep the economy moving ahead. And, given the outsized influence of the Federal Reserve, it could be said we have a coxswain that not only gives commands to the rowers, but also alters the river currents. That, as noted last month, makes it difficult for economists to call the outcome of the race.

Meanwhile, as expected, the pace of new vehicle sales leveled off. There were some signs that retail used vehicle sales may be doing the same. Nevertheless, the flow of funds into retail financing remains impressive and that will keep used vehicle sales at a healthy level. Wholesale used vehicle prices declined again in April, but the movement was neither unexpected nor disruptive to the market.

ECONOMY: MOVING AHEAD AT MODERATE SPEED

Retail Sales: Which number to believe? In April, retail sales were either up a scant 0.1% (total retail sales), up 0.7% (excluding gasoline), or down 0.1% (excluding autos). Our belief is that autos should always be excluded from the total sales numbers. They are volatile and they add no additional information since unit volumes have already been reported long before the retail sales report. Gasoline is a trickier issue. Always exclude gas when price spikes push dollar sales higher even when fewer gallons are sold. But, when gasoline prices decline (as they did in April) the analysis becomes more nuanced.



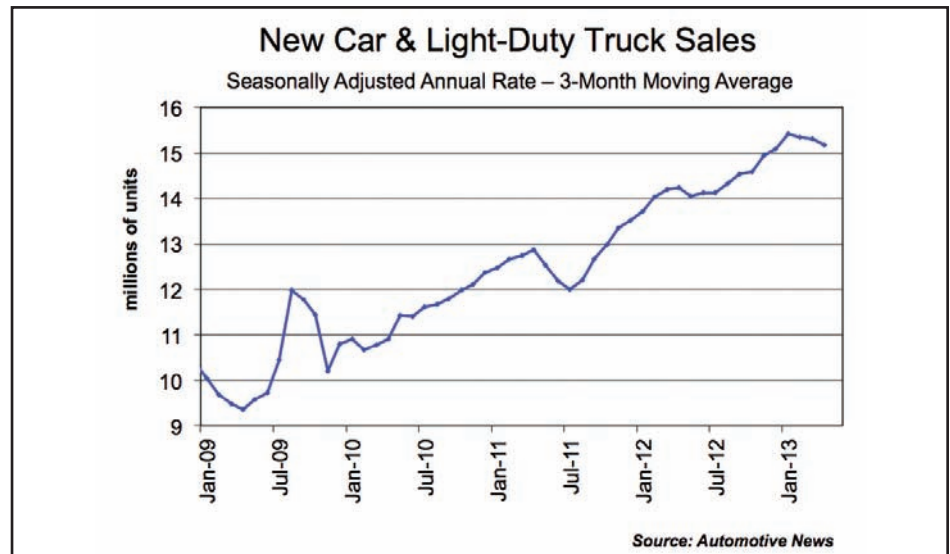
Sure, lower gas prices artificially reduce total retail sales numbers since energy purchases are somewhat inelastic, but, over time, one would hope that the increased purchasing power fueled by lower pump prices would work its way into other retail sectors. To date, evidence of that has not been clear. Retail sales, excluding gasoline, are rising at a respectable pace, but the gains are coming at the expense of a lower consumer savings rate.

To get a true sense of the psyche of many used vehicle buyers, it's probably best to concentrate on specific businesses and retail sectors, most notably Walmart, dollar stores, and casual dining restaurants. First quarter results and second quarter guidance from all of these sectors suggest that the financial health and confidence of most used vehicle buyers is improving only slowly. At Walmart, North American same-store sales declined for the first time in seven quarters and the CFO stated "our customers are still stretched." Results for casual dining establishments were, at best, lackluster.

We expect that the spending power and confidence of most used vehicle buyers will remain relatively subdued. After all, the biggest recent improvements in the economy have concentrated in the equity markets and home values. That helps higher-income households (new vehicle buyers), but mainstream America needs faster growth in weekly incomes.

RETAIL AND WHOLESALE VEHICLE MARKETS

New vehicle sales pace eases. In April, for the first time since October of last year, the seasonally adjusted annual selling rate for new cars and light-duty trucks slipped below 15 million. Although it is still generally expected that full-year sales will be closer to 15.5 million than 15.0 million, the consumer's low savings rates, coupled with only moderate income growth, suggests that manufacturers and dealers may have to become more aggressive in pushing the market to reach their full-year sales targets.



Used vehicle sales stable in April. Total used vehicle sales rose less than 1% in April, according to CNW. And, used vehicle retail sales by dealers (excluding private party transactions) fell by 1%. Nevertheless, sales for the first four months were up 5% in total, and up 7% for dealer sales. That's a noteworthy achievement in the face of otherwise tepid consumer spending. Clearly, the ample flow of retail credit is boosting the used vehicle market.

Results for the seven publicly traded dealership groups show that used unit retail sales rose 6.5% on a same-store basis in the first quarter of this year. That marked the 15th-consecutive quarterly increase. Unfortunately, gross margins continued to decline. On a sales-weighted basis, it was the 13th-consecutive quarter that used vehicle retail gross margins were lower than their year ago level. Given that F&I income is likely going to come under pressure, these narrow margins will prevent dealers from becoming aggressive bidders at auction.

MANHEIM CONSULTING
6205 Peachtree Dunwoody Rd.
Atlanta, GA 30328

678-645-2377
800-777-2053

www.manheim.com/consulting

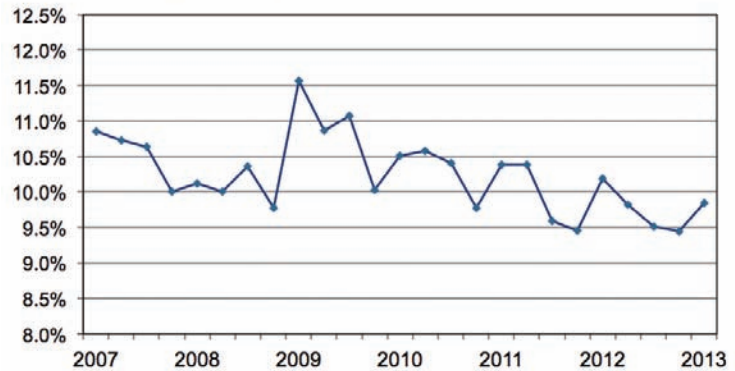
© 2013 Manheim Inc. All rights reserved.



Used Vehicle Retail Gross Margin

(Publicly-traded Dealership Groups)

Sales-weighted average for KMX *, AN, PAG, SAH, GPI, ABG, and LAD



*KMX shifted forward one month to correspond with calendar quarter

Source: Company filings

Manheim Index declines in April. Wholesale used vehicle prices (on a mix-, mileage-, and seasonally adjusted basis) declined 1.0% in April. This brought the Manheim Used Vehicle Value Index to a level of 119.2, which was 5.5% lower than a year ago.

Although April marked the fourth consecutive monthly decline in wholesale used vehicle values (and produced a cumulative decline of 3.9% since December), the recent movement has been neither alarming nor disruptive to the market. Indeed, the easing was long anticipated and, in fact, probably mitigates some of the decline that many were expecting for the back half of this year. Some evidence of that has already been seen; adjusted prices in the first 15 days of May were little changed from April. However, if used retail demand continues to moderate (and new vehicle incentives continue to rise), that will put further pressure on wholesale values.

Manheim Used Vehicle Value Index

January 1995 = 100



Source: Manheim Consulting

What \$5,000 will buy. Since this is the month for the major BHPH Convention, we have updated our analysis of what \$5,000 buys. It shows the average mileage for vehicles sold at auction between \$4,000 and \$6,000 for the time period between April 1 and May 15 of each year. (A \$5,000 vehicle acquisition cost is considered the sweet spot by many BHPH operators.)

MANHEIM CONSULTING
6205 Peachtree Dunwoody Rd.
Atlanta, GA 30328

678-645-2377
800-777-2053

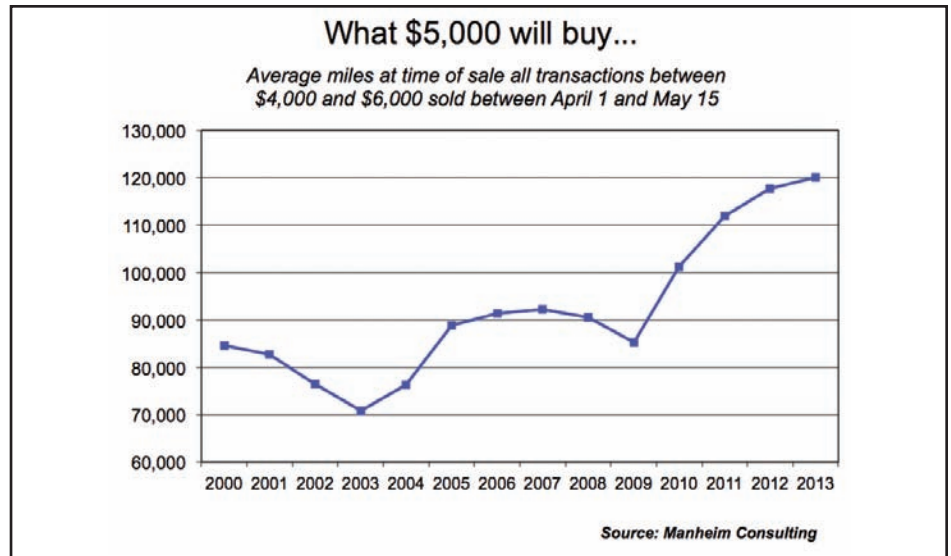
www.manheim.com/consulting

© 2013 Manheim Inc. All rights reserved.



If you spent \$5,000 at auction in 2003 you got, on average, a vehicle with 70,753 miles. This year, that same \$5,000 would have gotten you, on average, a vehicle with 120,024 miles. And this occurred even as the availability of used vehicles in the wholesale marketplace that are suitable for possible BHPH inventory increased in 2013. Blame the recent movement on increased demand. And that increased demand has not coming solely from BHPH dealers. As subprime and deep subprime lenders bought further down the credit scale, dealers who use these financing sources were increasingly competing against BHPH dealers for the same units.

Sure, vehicle quality and longevity have increased over the years – but not by that much! Selling vehicles with significantly higher mileage has forced BHPH dealers to adjust their business operations. For one, it requires more skill and effort devoted to buying in order to increase the likelihood that the vehicle will run the term of the note. The reputation of the seller that the dealer is buying from takes on added importance – as do post-sale inspections. And, even after instituting those practices, it would be prudent for the dealer to set aside larger reserves for future goodwill repairs in case of a mechanical breakdown during the term of the note.



MANHEIM CONSULTING
6205 Peachtree Dunwoody Rd.
Atlanta, GA 30328

678-645-2377
800-777-2053

www.manheim.com/consulting

© 2013 Manheim Inc. All rights reserved.



**Thomas Webb***Chief Economist*

Manheim Consulting

(540) 364-3735

Thomas.Webb@Manheim.com

Q. Financial markets seem to be more sensitive to possible Federal Reserve actions than ever. Why is that when the Fed is now in a new era of transparency?

A. Yes, it does seem to be contradictory. But, then again, whereas markets use to try to anticipate future Fed actions now they are anticipating future announcements of future actions. Not much difference there.

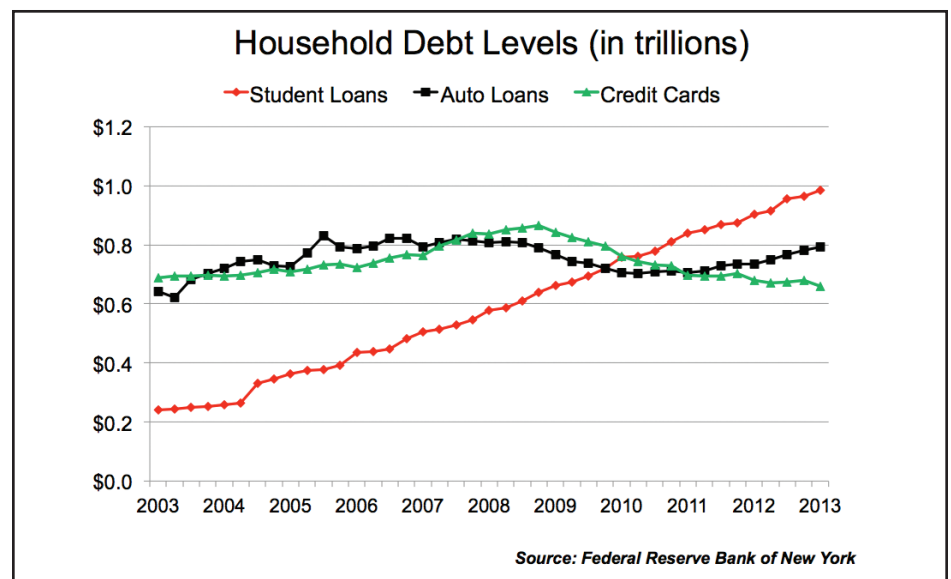
The reason for the Fed's outsized influence is that it now plays a much greater role in the economy's future direction. The Fed's policy of "whatever it takes, for as long as it takes" has put us in uncharted territory and left financial markets rightfully concerned.

Look for the Fed to remain transparent in communicating plans, but be flexible in shifting those plans. It's an attempt to mitigate some of the "rush-to-the-exit" problems that have inevitably occurred after every other major shift in Fed policy.

Q. I was stunned to read that student loan debt now exceeds all other forms of non-mortgage debt. With job prospects for current college graduates not all the great, this can't be a good thing, right?

A. Yes, throughout the recession and even during the current recovery consumers have de-levered. Credit card debt, which use to be the biggest form of non-mortgage debt, peaked at \$866 billion in the fourth quarter of 2008. It now stands at \$660 billion. Auto debt peaked at \$820 billion in late 2006, fell to \$710 billion during the recession, and has now stands at \$794 billion.

Meanwhile student loan debt escalated over the past decade without even a hiccup during the recession. Student loan debt outstanding, which was \$241 billion in 2003, is now nearly \$1 trillion.



A recent study shows that persons with student loans outstanding are less likely to buy a new vehicle than those without that debt overhang. As recently as two years ago, those with student debt were more likely to buy a new vehicle than those without such debt. That's because they had greater skills and higher incomes than the general population.

MANHEIM CONSULTING
6205 Peachtree Dunwoody Rd.
Atlanta, GA 30328

678-645-2377
800-777-2053

www.manheim.com/consulting

© 2013 Manheim Inc. All rights reserved.