

# Elevate Your Auto Lending Horizons with Competitive Attributes & Pricing

Gaining an Edge with Risk Based Pricing



# Today's Agenda

- Identify opportunities for Credit Unions to capture more of the auto lending market
- Pricing auto loans competitively using risk-based pricing and various risk attributes



On average a consumers  
preferred financial institution  
wins

**64%**

of all their purchases



On average a credit union  
member intends to give

**88%**

of all their future business to  
their credit union.



# Where do we fall short in auto lending?

Retail LTV	≤ 75%	≤ 80%	≤ 85%	≤ 90%	≤ 95%	≤ 100%	≤ 105%	≤ 110%	≤ 115%	≤ 120%	≤ 125%	≤ 130%
Trade LTV	≤ 90%	≤ 95%	≤ 100%	≤ 105%	≤ 110%	≤ 115%	≤ 120%	≤ 125%	≤ 130%	≤ 135%	≤ 140%	≤ 145%
750 +												
700 - 749												
680 - 699												
660 - 679												
640 - 659												
620 - 639												
600 - 619												
580 - 599												
560 - 579												

# Non-Prime Members in Mind

Retail LTV	≤ 75%	≤ 80%	≤ 85%	≤ 90%	≤ 95%	≤ 100%	≤ 105%	≤ 110%	≤ 115%	≤ 120%	≤ 125%	≤ 130%
Trade LTV	≤ 90%	≤ 95%	≤ 100%	≤ 105%	≤ 110%	≤ 115%	≤ 120%	≤ 125%	≤ 130%	≤ 135%	≤ 140%	≤ 145%
750 +	250	294	384	449	528	571	534	817	192	229	50	93
700 - 749	732	1016	1408	1572	1837	1913	1869	2580	841	1450	171	289
680 - 699	640	953	1248	1587	1888	2011	1861	2713	1083	1872	161	297
660 - 679	872	1175	1657	2047	2331	2681	2677	3950	3455	316	587	
640 - 659	1169	1755	2503	3089	3512	3947	4280	6223	5656	461	854	
620 - 639	1326	1935	2769	3398	4099	4664	4791	7407	6377	497	849	
600 - 619	1278	1917	2674	3344	3916	4404	4647	10659	461	852		
580 - 599	997	1477	2061	2461	2849	3181	3240	6975	312	616		
560 - 579	372	502	723	1052	1257	2696	305	578				

Source: Lenders Protection portfolio of 1.6 million applications over a 10-year period



# The Non-prime Members Demographic

- Limited Credit Experience
- Single major credit problems (usually driven by medical problems or a divorce)
- Lack access to money in savings
- Typically not rate sensitive
- Monthly payment driven



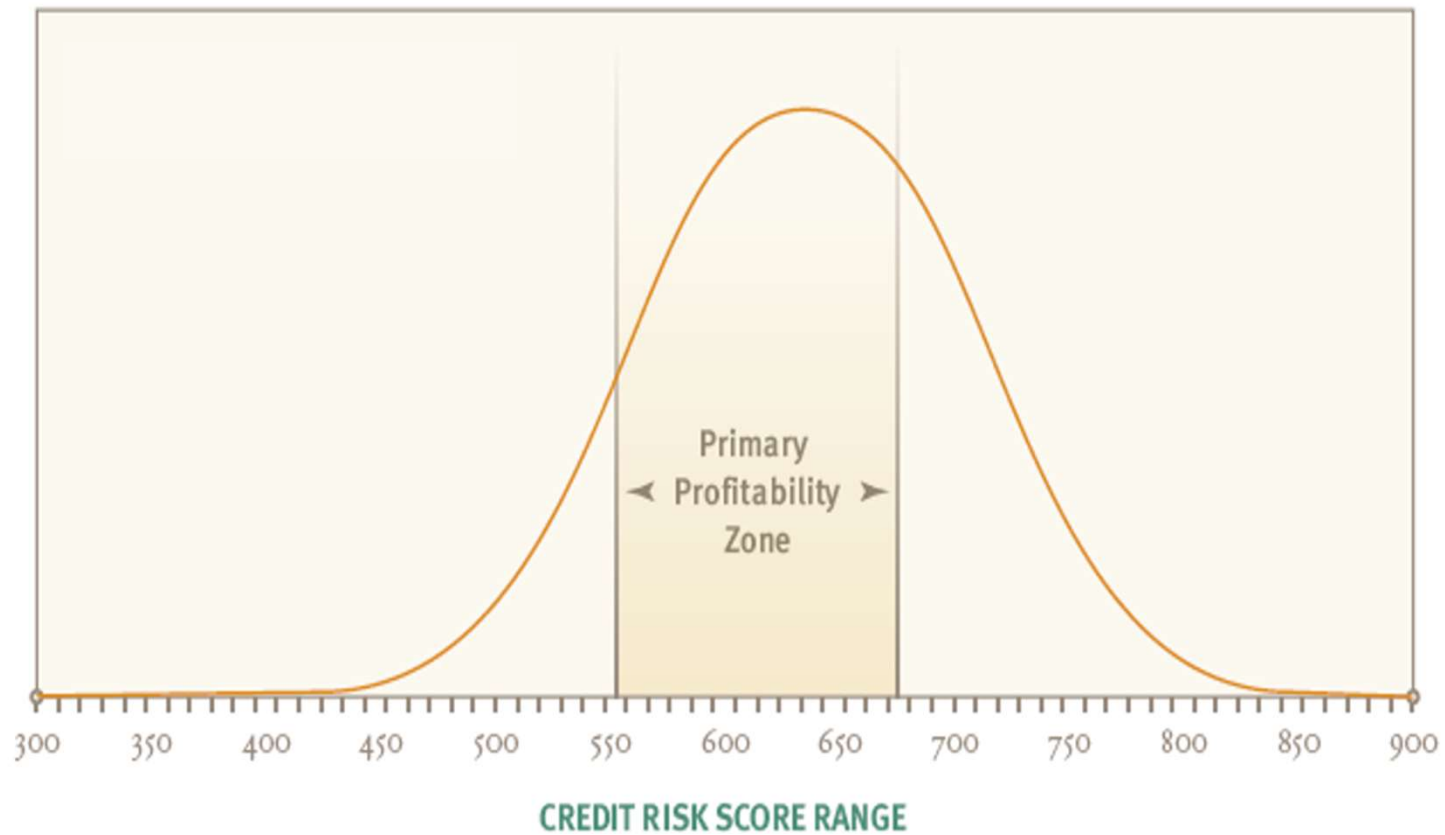
# Worth the risk?

- Approve and book more loans
- Increase Profitability
- Enhance member relationships
- Attract new members
- Serve the underserved





# Profitability Zone in Auto Lending



# How do we price for the increased risk?

Interest Rate Pricing Strategies



# Common Issues Today

- Lending rates are usually a function of there competitive environment, with rates being set at whatever the market will bear
- The competition is making loans at irrational levels, making it more difficult to offer products/pricing that will be attractive to members and ensure profitability
- Ability to price loans competitively and accurately for non-prime members



# Costs Associated with an Auto Loan



## Cost of Funds

Deposits or borrowing money  
Average of all credit unions = 0.53%



## Loan Servicing

Cost to service and collect on loan  
May vary by tier  
Loss provision



## Marketing Expense

Dealer flats  
Origination expenses



## Return on Assets

Net return to credit union after all expenses



# True Risk Based Pricing Methodology

- Allows lenders to **price individual loans** based on a wide range of characteristics, including credit criteria and many other different risk attributes.
- Key Element to true risk-based pricing: ***Takes into account not only probability of defaults, but severity.***



# RISK ATTRIBUTES

Contributors to Risk

CREDIT SCORE



ORIGINATION CHANNEL



CREDIT DEPTH



LOAN TERM



NEW / USED



LOAN TO VALUE



VEHICLE MAKE / MODEL



GEOGRAPHIC LOCATION



# Find the Highest Default Risk

<b>BORROWER</b>
<b>640</b>
<b>CREDIT UNION</b>
125% Loan to Value
72 Month Term
Used Vehicle
Indirect Channel
Default Rate

<b>BORROWER</b>
<b>600</b>
<b>CREDIT UNION</b>
115% Loan to Value
72 Month Term
Used Vehicle
Indirect Channel
Default Rate

<b>BORROWER</b>
<b>560</b>
<b>CREDIT UNION</b>
125% Loan to Value
72 Month Term
Used Vehicle
Direct Channel
Default Rate

# Find the Highest Default Risk

<b>BORROWER</b>
<b>640</b>
<b>CREDIT UNION</b>
125% Loan to Value
72 Month Term
Used Vehicle
Indirect Channel
18%

<b>BORROWER</b>
<b>600</b>
<b>CREDIT UNION</b>
115% Loan to Value
72 Month Term
Used Vehicle
Indirect Channel
26%

<b>BORROWER</b>
<b>560</b>
<b>CREDIT UNION</b>
125% Loan to Value
72 Month Term
Used Vehicle
Direct Channel
24%



# How depreciation speeds affect yields

## Chrysler

\$25,000 loan amount

\$20,000 vehicle value

10% Interest Rate

Defaults in month 13

Depreciation rate 72%

\$20,586.65 Deficiency Balance

\$14,400 vehicle value at default

\$6,186.65 Deficiency After Sale

## Toyota

\$25,000 loan amount

\$20,000 vehicle value

10% Interest Rate

Defaults in month 13

Depreciation rate 82%

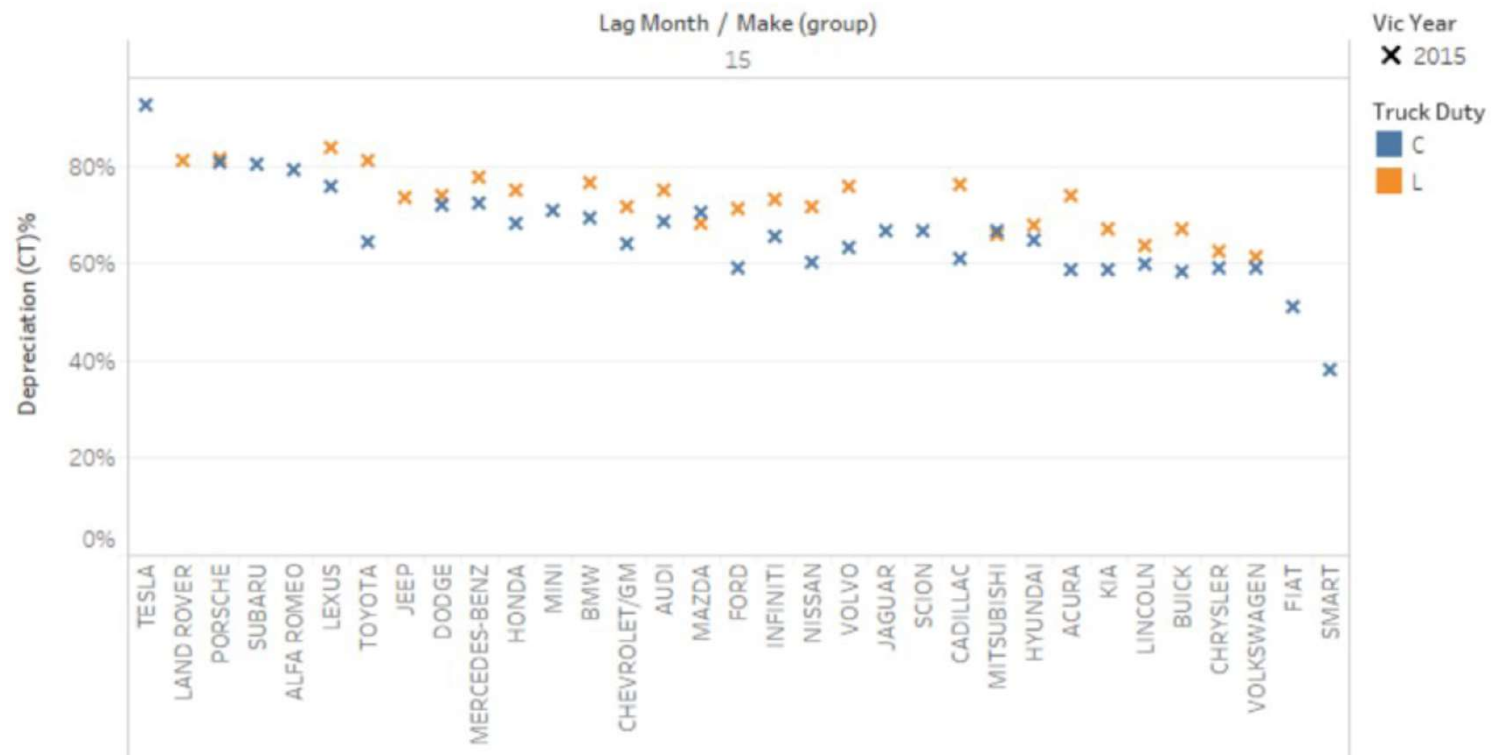
\$20,586.65 Deficiency Balance

\$16,400 vehicle value at default

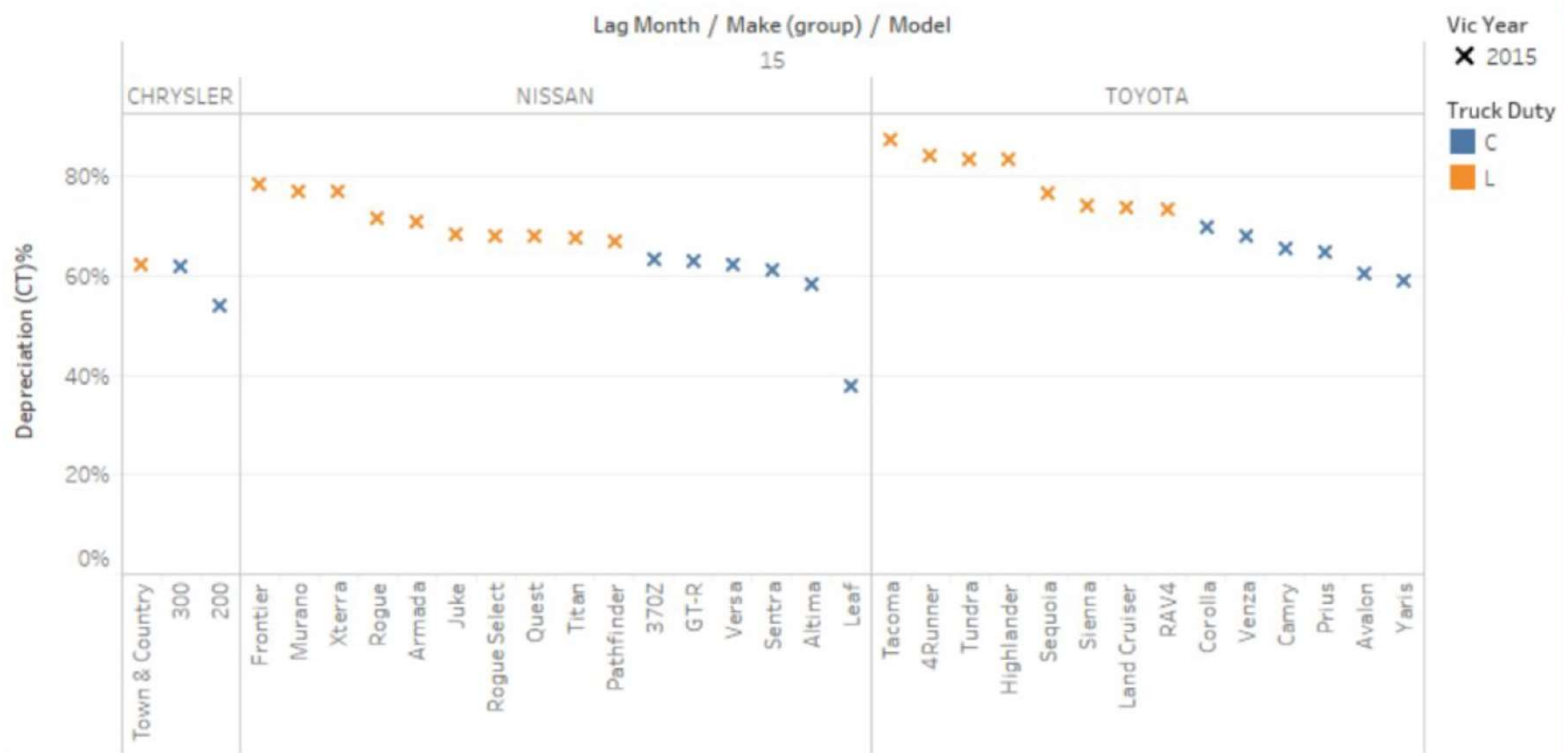
\$4,186.65 Deficiency After Sale



# Measure for Severity of Loss



# Measure for Severity of Loss



# Find the Highest Default Risk

<b>BORROWER</b>
<b>580</b>
<b>CREDIT UNION</b>
95% Loan to Value
72 Month Term
Used Vehicle
Thick File
Default Rate

<b>BORROWER</b>
<b>600</b>
<b>CREDIT UNION</b>
110% Loan to Value
60 Month Term
New Vehicle
Normal File
Default Rate

<b>BORROWER</b>
<b>580</b>
<b>CREDIT UNION</b>
115% Loan to Value
72 Month Term
Used Vehicle
Thin Channel
Default Rate

# Find the Highest Default Risk

<b>BORROWER</b>
<b>580</b>
<b>CREDIT UNION</b>
95% Loan to Value
72 Month Term
Used Vehicle
Thick File
15%

<b>BORROWER</b>
<b>600</b>
<b>CREDIT UNION</b>
110% Loan to Value
60 Month Term
New Vehicle
Normal File
33%

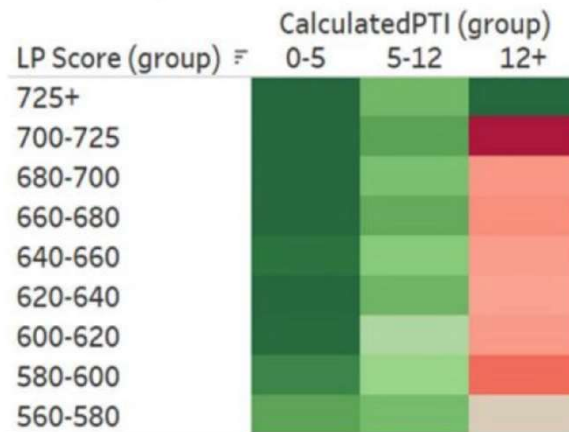
<b>BORROWER</b>
<b>580</b>
<b>CREDIT UNION</b>
115% Loan to Value
72 Month Term
Used Vehicle
Thin Channel
32%

# Payment to Income Ratios

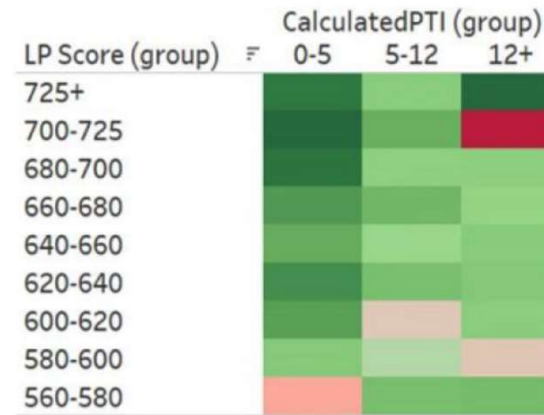
- Major contributor to default speeds



Loss Ratio by Calculated PTI



Calculated PTI Adjusted Loss Ratio



Source: Lenders Protection portfolio of \$6 billion in non-prime auto loans

# Find the Highest Default Risk

<b>BORROWER</b> <b>640</b> <b>CREDIT UNION</b>
125% Loan to Value
72 Month Term
Used Vehicle
Thick File
Default Rate

<b>BORROWER</b> <b>640</b> <b>CREDIT UNION</b>
125% Loan to Value
72 Month Term
Used Vehicle
Normal File
Default Rate

<b>BORROWER</b> <b>640</b> <b>CREDIT UNION</b>
125% Loan to Value
72 Month Term
Used Vehicle
Thin File
Default Rate

# Find the Highest Default Risk

<b>BORROWER</b> <b>640</b> <b>CREDIT UNION</b>
125% Loan to Value
72 Month Term
Used Vehicle
Thick File
15%

<b>BORROWER</b> <b>640</b> <b>CREDIT UNION</b>
125% Loan to Value
72 Month Term
Used Vehicle
Normal File
20%

<b>BORROWER</b> <b>640</b> <b>CREDIT UNION</b>
125% Loan to Value
72 Month Term
Used Vehicle
Thin File
23%





Results															
Origin		Contract Rates													
Indirect		Stress Results													
New or Used		Loan to Value													
Used		Fico	Depth	0-80	81-85	86-90	91-95	96-100	101-105	106-110	111-115	116-120	121-125	126-130	131-135
750+	THICK	6.1%	6.1%	6.1%	6.1%	6.1%	6.1%	6.1%	6.3%	6.5%	6.7%	7.1%	7.5%	8.1%	
	NORMAL	6.2%	6.3%	6.3%	6.3%	6.3%	6.3%	6.3%	6.6%	6.9%	7.2%	7.6%	8.2%	8.9%	
	THIN	6.5%	6.5%	6.5%	6.5%	6.5%	6.5%	6.6%	6.9%	7.2%	7.6%	8.2%	8.9%	9.8%	
700-749	THICK	6.2%	6.2%	6.2%	6.2%	6.2%	6.3%	6.5%	6.7%	7.0%	7.4%	7.9%	8.4%		
	NORMAL	6.4%	6.4%	6.4%	6.4%	6.4%	6.5%	6.8%	7.1%	7.5%	8.0%	8.6%	9.3%		
	THIN	6.7%	6.7%	6.7%	6.7%	6.7%	6.8%	7.1%	7.6%	8.0%	8.6%	9.3%	10.2%		
680-699	THICK	6.4%	6.5%	6.5%	6.5%	6.5%	6.8%	7.0%	7.4%	7.8%	8.2%	8.7%	9.3%		
	NORMAL	6.6%	6.7%	6.7%	6.7%	6.8%	7.1%	7.5%	7.9%	8.4%	9.0%	9.6%	10.4%		
	THIN	6.9%	6.9%	6.9%	6.9%	7.1%	7.5%	7.9%	8.4%	9.0%	9.8%	10.5%	11.5%		
660-679	THICK	6.7%	6.8%	6.8%	7.0%	7.2%	7.5%	7.8%	8.2%	8.5%	8.9%	9.4%			
	NORMAL	7.0%	7.0%	7.0%	7.2%	7.6%	7.9%	8.4%	8.8%	9.3%	9.8%	10.4%			
	THIN	7.2%	7.2%	7.2%	7.5%	7.9%	8.4%	8.9%	9.5%	10.0%	10.7%	11.4%			
640-659	THICK	7.1%	7.1%	7.2%	7.5%	7.8%	8.2%	8.6%	9.0%	9.4%	9.9%	10.4%			
	NORMAL	7.3%	7.3%	7.5%	7.8%	8.2%	8.7%	9.2%	9.8%	10.3%	10.9%	11.5%			
	THIN	7.5%	7.6%	7.8%	8.2%	8.7%	9.3%	9.9%	10.6%	11.2%	12.0%	12.7%			
620-639	THICK	7.7%	7.7%	7.9%	8.2%	8.6%	9.1%	9.6%	10.0%	10.5%	10.9%	11.3%			
	NORMAL	7.9%	8.0%	8.2%	8.7%	9.2%	9.8%	10.5%	11.1%	11.6%	12.2%	12.8%			
	THIN	8.3%	8.3%	8.6%	9.2%	9.8%	10.6%	11.3%	12.1%	12.7%	13.4%	14.1%			
600-619	THICK	8.1%	8.1%	8.3%	8.7%	9.2%	9.8%	10.3%	10.9%	11.4%	11.9%				
	NORMAL	8.4%	8.5%	8.7%	9.3%	9.9%	10.6%	11.3%	12.1%	12.7%	13.4%				
	THIN	8.7%	8.8%	9.1%	9.8%	10.6%	11.4%	12.3%	13.2%	14.0%	14.9%				
580-599	THICK	8.6%	8.7%	8.9%	9.4%	9.9%	10.5%	11.2%	11.8%	12.4%	13.0%				
	NORMAL	9.0%	9.0%	9.3%	10.0%	10.7%	11.5%	12.4%	13.2%	13.9%	14.7%				
	THIN	9.4%	9.4%	9.8%	10.6%	11.5%	12.5%	13.5%	14.5%	15.3%	16.3%				
560-579	THICK	9.3%	9.3%	9.6%	10.2%	10.9%	11.7%	12.5%	13.3%						
	NORMAL	9.7%	9.8%	10.2%	11.0%	11.9%	13.0%	14.0%	15.0%						
	THIN	10.2%	10.3%	10.7%	11.7%	12.9%	14.1%	15.4%	16.7%						

Default  
Freq – 13%  
Prepay  
Freq – 42%

Default  
Freq – 17%  
Prepay  
Freq – 42%

Default  
Freq – 20%  
Prepay  
Freq – 43%



# Summary

- Accurately pricing risk ensures the long-term viability of an institution's ability to withstand the unpredictability of the economy and provide an advantage over competition.
- Lenders can position themselves as leaders in their markets for their ability to accurately price loans and serve a wider range of members.
- By building an auto portfolio whereby each loan is priced appropriately for risk, the overall net yields are much higher and loan volume increases without having to cut interest rates to the bone.
- One of the strongest arguments for having a risk-based pricing model is to facilitate restructuring in ways that are "win-win" for both the institution and its members.



SAY YES TO MORE AUTOMOTIVE LOANS



THANK YOU!

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