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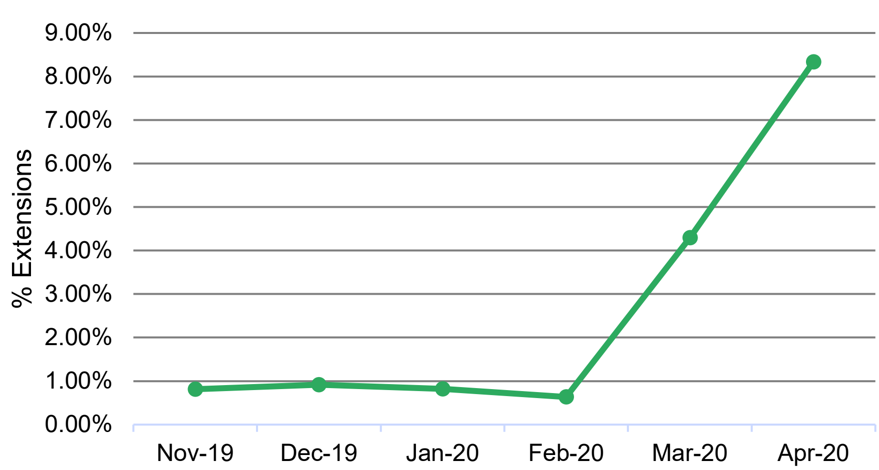
Recent Loan-Level Data Exposes the Prevalence of Extensions in Auto ABS

With the unprecedented COVID-19 crisis causing a rapid rise in unemployment rivaling levels not seen since the Great Depression, investors have been asking: How will securitizations that depend on consumer outlook perform? How will these markets look to migrate such risks? This paper explores how the US Auto asset-backed security (ABS) market has responded to the crisis through the elevated use of loan extensions. By analyzing available auto loan-level data through Moody's Analytics DataViewer (which displays monthly auto loan-level data required by the SEC to be reported under Regulation AB II), we highlight the current use of extensions by the market to mitigate these risks and the potential consequences this can introduce.

One of the main adjustments that the auto market has used to moderate the impact of the coronavirus crisis for the borrower is extensions. Extensions enable borrowers to skip a certain number of monthly payments that are then added back as additional payments at the end of the loan term. This offers relief to the borrower for an immediate short-term period, but also extends the borrower's loan maturity date by the number of postponed payments. Figure 1 depicts a significant increase of 583% in the use of extensions within our dataset from February (0.63%) to March (4.3%) at the onset of the crisis. Additionally, April's (8.3%) monthly extension utilization increased as well, coinciding with states beginning to implement lockdown procedures, causing a decrease in business activity and a correlated sharp increase in unemployment.

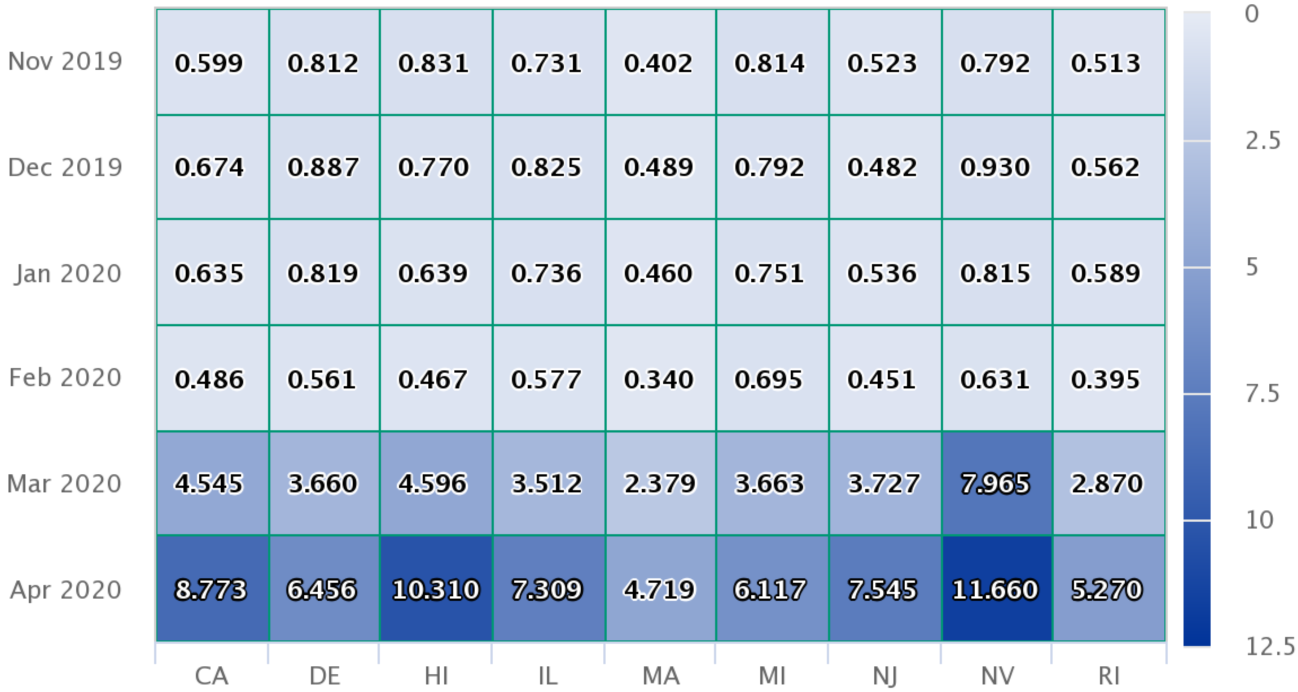
Figure 1 US auto loan extensions



Source: EDGAR/Moody's Analytics DataViewer

While extensions overall in the United States have drastically increased, we can also view the impact of extensions on a state-by-state basis. Figure 2 shows the states that had greater impact on unemployment levels and the use of extensions in these states. While all states have experienced an increase in unemployment and the use of extensions, we highlight those states with high unemployment. California, a state that on average represents a larger percentage in securitization pools, experienced an almost 9% extension rate increase at the end of April, which was significantly higher than the 0.64% rate in January. Additionally, Nevada and Hawaii, whose economies depend heavily on tourism that was affected by the crisis, also share some of the highest extension rates. Nevada alone from February to March had an increase in its extension rate from 0.63% to 7.97%, a twelve-fold increase in one month.

Figure 2 Extension percentage in states with high unemployment



Source: EDGAR/ Moody's Analytics DataViewer

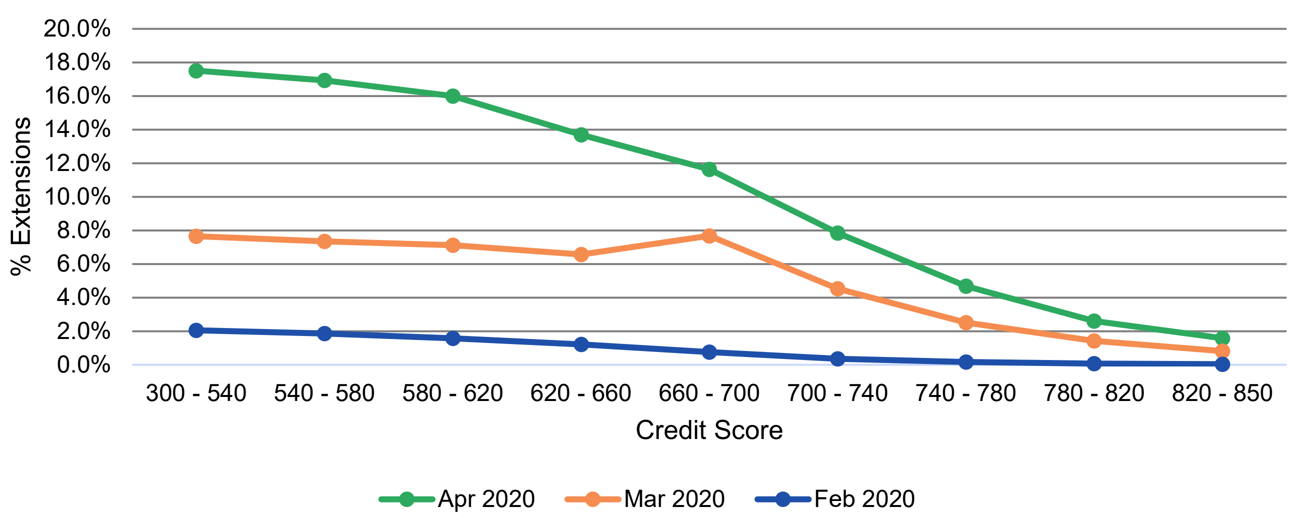
Multiple state governments decided to respond to the pandemic by offering residents protection from creditors, including temporarily barring repossessions. The National Consumer Law Center lists the states and territories that are currently extending this benefit. However, as shown in Figure 3, extensions are also continuing to increase and these areas are no exception. For example, from January to April, loan extensions increased from 0.74% to 7.3%.

Figure 3 States that temporarily paused repossessions

Source: EDGAR/Moody's Analytics DataViewer

Besides analyzing the loans on a state level, the dataset provides the ability to group extensions by borrower characteristics, such as credit score. When examining the pairing between extensions and credit scores in Figure 4, we note that borrowers with lower credit scores have a substantial number of extensions, which is to be expected. Borrowers with a credit score below 620 exhibited a higher than 15% extension rate in April 2020. Second, borrowers who are considered more prime also experienced a surge in extensions. For the FICO range of 700 to 780, the percentage of loans extended during April were 5% or higher—an increase from less than 1.0% in February. Overall, the loan-level data interestingly reveals that the effects of the COVID-19 crisis have not been limited to lower-tier credit score borrowers.

Figure 4 Extension percentage by credit score

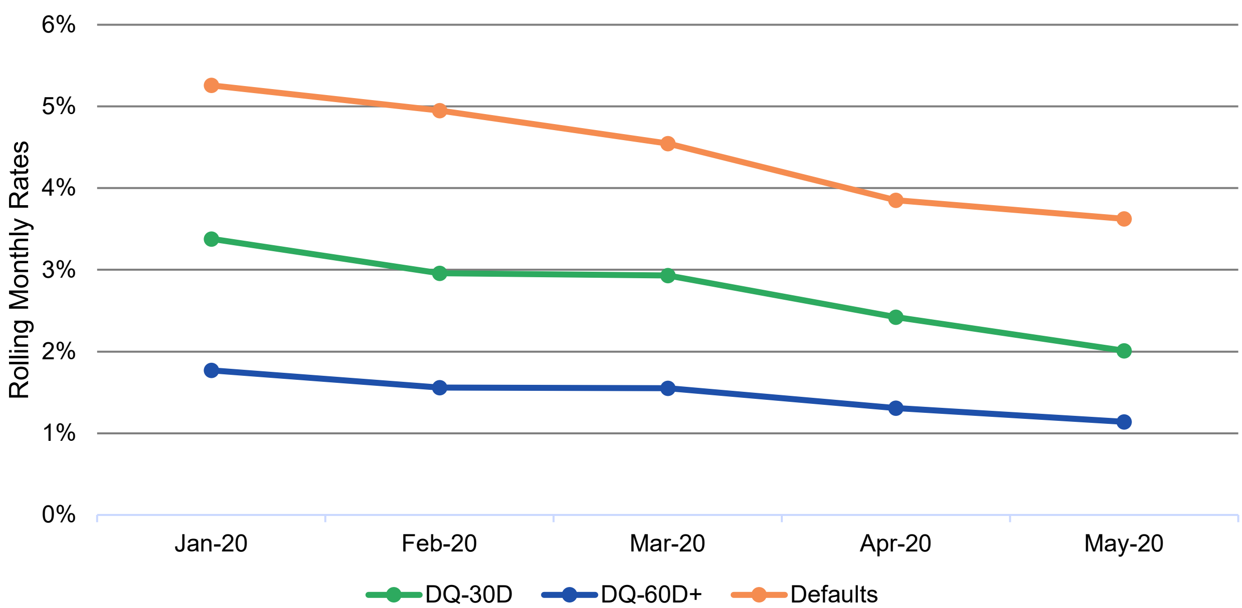


Source: EDGAR/Moody's Analytics DataViewer

Typically, metrics such as delinquencies and defaults are performance indicators for auto loan pools. Figure 5 shows some monthly performance data since the onset of the pandemic for auto loan securitization pools, which can be found in Moody's Analytics Structured Finance Portal. As noted, default and delinquency performance has remained steady or slightly improved month over month. An interesting point to observe is if the increased use of extensions might be delaying the impact of the crisis on these metrics. Once a borrower can no longer defer payments, delinquencies and defaults may begin to reflect the full effect of the pandemic and the associated consequences.

Additionally, the use of extensions might also affect the overall weighted average life of these pools as payments are added to the end of the loan. Extensions use could delay the timing of when to call these transactions. Such a delay could potentially negatively affect the weighted average lives of certain securitization tranches.

Figure 5 Figure 5: Auto loans – delinquencies and defaults



Source: Moody's Analytics / Structured Finance Portal

In conclusion, the auto market's use of extensions has grown rapidly with the onset of the pandemic and with the rise in unemployment. As we have noted, extension use has increased thirteen-fold from February to April 2020. When we drill down further by credit score, we note that even high credit quality borrowers have experienced an increased use of extensions—but not as high as lower credit quality borrowers. While using extensions may have, in the short term, alleviated borrowers' financial constraints and an uptick in the auto market's performance metrics, their impact perhaps has not yet been fully realized within the sector's securitization pools. Only time will tell.