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Q2 2020 General Motors Financial Company Inc Earnings Call - Prerecorded

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PRESENTATION

Stephen Jones ***General Motors Financial Company, Inc. - VP of IR***

Welcome to GM Financial's Second Quarter 2020 Earnings Presentation. This is Steve Jones, Vice President of Investor Relations at GM Financial. With me today are Dan Berce, President and CEO of GM Financial; and Susan Sheffield, Chief Financial Officer.

Before we proceed, I must remind everyone that the topics we will discuss during this presentation will include forward-looking statements, which are the company's current views with respect to future events and financial performance. These forward-looking statements are subject to many assumptions, risks and uncertainties that could cause actual results to differ significantly from historical results or from those anticipated by us. The most significant of these risks are detailed from time to time in the company's filings and reports with the Securities and Exchange Commission, including the annual report on Form 10-K for the year ended December 31, 2019. If one or more of these risks or uncertainties materialize or if the underlying assumptions prove incorrect, our results may vary materially.

If you have questions on the material discussed, please feel free to contact me. My contact information can be found on both the earnings release and at the end of the presentation slides. We will be posting a transcript of this presentation to our website.

I will now turn the call over to Dan Berce. Dan?

Daniel E. Berce ***General Motors Financial Company, Inc. - President & CEO***

Thanks, Steve.

I'll start out with financial and operating highlights for our second quarter of 2020. GMF earned $226 million in the second quarter, down from $536 million in the second quarter a year ago. As Susan will explain in more detail, the decline in earnings is primarily due to higher credit provisions for loss expectations associated with the impact of COVID-19 and accelerated depreciation expense due to expected lower residual values.

We experienced strong loan originations in the U.S. in the second quarter, with higher retail penetration levels due to favorable GM incentive programs and effective dealer engagement. Total originations, however, were down year-over-year as leasing volume declined with the temporary closure of dealerships in key markets and Latin American originations negatively impacted by pandemic lockdowns.

Earning assets declined year-over-year due to runoff of our floorplan book, due to suspension of manufacturing operations. Our U.S. floorplan market share has now exceeded 30%.

Turning to credit. Retail net charge-offs in the second quarter of 2020 were only slightly impacted by the effects of COVID-19. Retail credit metrics are expected to weaken in the second half of the year.

From a customer experience standpoint, for the fourth consecutive year, GM Financial was #1 in manufacturer loyalty.

We continue to be active in our funding platforms, issuing $8.2 billion in public and private debt securities and renewing 13 credit facilities totaling $13.2 billion.

And we paid another $400 million dividend to GM in June, bringing the year-to-date total to $800 million.

Next slide, retail loan originations and portfolio balance. Retail loan originations were strong in the quarter at $8.7 billion, led by a record $6.9 billion of financing of new GM vehicles. GM's 0% financing offers plus effective dealer engagement drove this growth and resulted in a higher credit profile at origination. Our used car origination volumes were also up year-over-year, while Latin American volumes were down.

Next slide, retail loan credit performance. Early stage delinquency rates in the U.S. declined for the second quarter of 2020 compared to the first quarter due primarily to government stimulus, lower consumer spending and GM Financial customer support programs. The payment deferrals we made during the pandemic period also positively impacted delinquency as accounts are generally brought current through the deferment process.

I'll give some stats on the deferments we did during the pandemic period. During the period from about mid-March through the end of June, we deferred 127,000 accounts. Statistics for those accounts as of last Sunday, July 26 are: 80% made their scheduled payment by the due date. 5% have not yet had a due date. 1% received an additional payment deferral. And the remainder, roughly 14%, are at least one day past due. We do expect delinquency and net charge-offs to increase in the second half of the year with the perhaps expiration of government support programs, continued elevated unemployment rate, weaker performance in Latin America, the recent increase in the spread of COVID-19 and normal seasonal trends. We expect annual net charge-offs to range between 2% and 2.5% for the full year 2020.

Next slide, operating lease originations and portfolio balance. Our lease volumes were $3.2 billion in the second quarter, down considerably due to dealership closures and pandemic lockdowns in large lease markets such as Michigan and New York. GM's strong loan incentives also contributed to the shift away from leasing. Our lease portfolio remains a high-credit-quality book with low delinquency at quarter end.

Next slide, GM Financial used car trends. This chart, while busy, shows graphically the volatility of the used car market since the start of the pandemic. Used car auction volumes and pricing troughed in early April and then rebounded strongly throughout the rest of the quarter. Favorable trends have continued late into July. That said, we do expect headwinds as far as used car pricing in the second half of the year from increased off-lease supply, increased repossession activity and rental car depleting, weaker demand as inventory and trade-ins increase, economic uncertainty and historical seasonal weakness in used vehicle pricing. We will continue to accelerate depreciation expense consistent with an industry forecast of a 6% to 8% decline in used vehicle prices in 2020 compared to 2019, which is a slight improvement from the previous estimate of a 7% to 10% decline due to that recent market strength.

Next slide, commercial lending. Our commercial receivables portfolio is down by over $5 billion year-over-year primarily from the suspension of manufacturing operations and better-than-expected sales performance in the U.S. As I mentioned before, our U.S. floorplan penetration continues to climb, reaching above 30% at the end of the quarter. Dealer health remains stable due to prudent expense management, support programs offered by GM Financial, and the availability of government funding such as the Paycheck Protection Program in the U.S.

And my last slide deals with data from our China joint ventures. While our penetration of SGM retail sales remained strong, we did see a sizable increase in our penetration of SGMW sales in the quarter. Retail contract origination volume in numbers was strong with a 5% year-over-year increase, but the dollar volume of originations was lower, impacted by our increasing mix of lower-cost SGMW vehicles. Credit in China is stabilizing in the quarter at a 50 basis point loss rate. And our second quarter equity income was up from the first quarter as China's recovery from the economic impacts of the pandemic continues to outpace our other markets.

And now I'll turn it over to Susan.

Susan B. Sheffield ***General Motors Financial Company, Inc. - Executive VP & CFO***

Thanks, Dan.

For the 3 months ended June 30, 2020, earnings before tax was $226 million, down $310 million from the prior year June quarter. The lower EBT year-over-year was driven primarily by reduced revenue on the commercial loan portfolio and lease portfolio, increased leased vehicle expense and loan provision, offset by a reduction in interest expense. For a little more detail, revenue was down $216 million primarily due to lower lease vehicle income due to the reduction in the portfolio and reduced finance charge income due to the decline in the commercial finance receivables balance, which Dan talked about.

Total expenses were $94 million higher in the quarter. Leased vehicle expense increased due to the expected lower residual values on the lease assets requiring accelerated depreciation expense, which was up $142 million year-over-year. With respect to provision expense, the provision expense increased $148 million year-over-year, of which $93 million is related to the economic forecast changes due to COVID. The balance is related to Q2 activity and the higher retail loan originations that Dan mentioned. We'll take a closer look at the allowance for retail losses on the next slide.

These items were offset by interest expense, which was down $164 million due to the falling benchmark interest rates. Our effective interest rate on debt declined 80 basis points to 3.3% compared to 4.1% a year ago.

For the calendar year of 2020, we still expect the EBT to be lower than 2019 due to the decline in used vehicle prices driving accelerated depreciation and the increased provision expense related to the current economic conditions and our outlook due to the pandemic.

Now turning to the allowance for retail loan losses. The allowance for retail loan losses was $2 billion, up from $1.9 billion at the end of Q1 2020 and up from [$881 million] (corrected by company after the call) a year ago. The allowance as a percent of consumer finance receivables was 4.4% at quarter end, up from 2.1% a year ago.

As a reminder, under the new current expected credit losses methodology, there are significant changes from the previous methodology. First, now the reserve must cover lifetime losses at origination. And second, it includes an economic forecast component, which is over the lifetime of the portfolio as well.

Based on the allowance process, we needed $2 billion in reserves for the consumer loan portfolio at the end of June to cover lifetime losses. Charge-offs in the quarter were $256 million, offset by recoveries of $89 million in the quarter.

I'll note that recoveries were lower than the previous quarters due to the temporary suspension of repossession activity during the second quarter. The provision for losses then is the build to get to our required allowance. It included establishing coverage for new originations based on lifetime losses on loans originated in the quarter, trends in the current credit performance, and the impact of the economic assumptions. The economic impact for the June 2020 quarter allowance build was $91 million for this retail loan allowance. And as a reminder, the Q1 2020 quarter had an economic impact attributed to the allowance build of $228 million.

Turning to the balance sheet on Slide 12. Ending earning assets were down slightly due to the reduction in commercial receivables that we mentioned earlier, and lower lease assets due to the lower lease activity that Dan mentioned. Our retail receivables grew due to the record origination volume and was almost 50% of total ending earning assets at the end of the quarter.

Total debt was $92.3 billion at the end of June 2020. And we exceeded our 50% target of unsecured debt at 56%. Debt was higher year-over-year and compared to year-end due to the shift in our liquidity position to more cash.

Our liquidity was strong at the end of the quarter at $25 billion and in line with our target of carrying at least 6 months' worth of liquidity to support cash needs over that time frame without access to capital markets. The composition shifted to more cash in late March and continuing in early Q2 as we utilized our credit facilities in response to the uncertainty in the global markets and weak economic environment. As the U.S. capital markets began to show strength and we were able to successfully access the capital markets as well as renew many of our credit facilities, we began paying down the credit facilities and shifting our liquidity composition back to a more normal bifurcation between credit facilities and cash.

Speaking of funding on Slide 13. Despite the challenging environment, we had a very active quarter across our funding platform. We renewed $13.2 billion of credit facilities in the quarter and have $26 billion in committed credit facilities provided by 27 banks. We raised over $8 billion in permanent financing in the quarter issuing off our public ABS platforms and our senior unsecured note platform. We complemented these permanent funding activities with closing several private amortizing securitizations. And subsequent to quarter end, we raised $1 billion off our subprime ABS platform, and that transaction closed earlier this month.

Turning to an update on our public issuance plans on Slide 14. You can see we are well on track for this year's funding activity. As always, the amount is going to be dependent on market conditions and the pace of our new asset origination.

Turning to our capital position on Slide 15. Tangible net worth declined from December due to the adoption of CECL, which was an equity impact of $643 million; the impact of the stronger U.S. dollar, which negatively impacts our investment in non-U.S. subsidiaries; and the dividend paid to GM; offset by the net income we earned in the first half. Importantly, our leverage ratio remains below our managerial target of 10x. And we have a capital cushion of $1.8 billion before exceeding the Support Agreement leverage ratio limit of 11.5x. This cushion supports a doubling of both our annual -- our current expected annual retail net charge-offs, which is a range of 2% to 2.5%, and a used vehicle price decline of 6% to 8% before exceeding the Support Agreement ratio.

Our return on average tangible common equity was down primarily due to lower earnings in the first half of the year.

Overall our performance in the quarter was, as Dan said, better than expected. Retail origination volume was a record high for the quarter. And our penetration of GM retail sales was over our target of 50%. Used car prices rebounded and credit performance certainly has performed well for the reasons we discussed.

Our access to funding was strong, supported by the U.S. government's quick attention to keeping liquidity flowing in a very challenging environment. Our balance sheet, capital and liquidity position set us up well to navigate the potential headwinds. We'll continue our disciplined strategy so that we can continue to support our customers, dealers, GM and our team members. Our team members are doing an amazing job being flexible and executing in this new work environment.

Thank you for your continued support of GM Financial. I'll turn the call back to Steve.

Stephen Jones ***General Motors Financial Company, Inc. - VP of IR***

Thank you, Susan.

This concludes GM Financial's Second Quarter 2020 Earnings Presentation. If you have questions, please feel free to contact me. As mentioned, my contact information can be found on both the earnings release and at the end of the presentation slides. Thank you for your continued interest and support of GM Financial. Have a nice day.
