

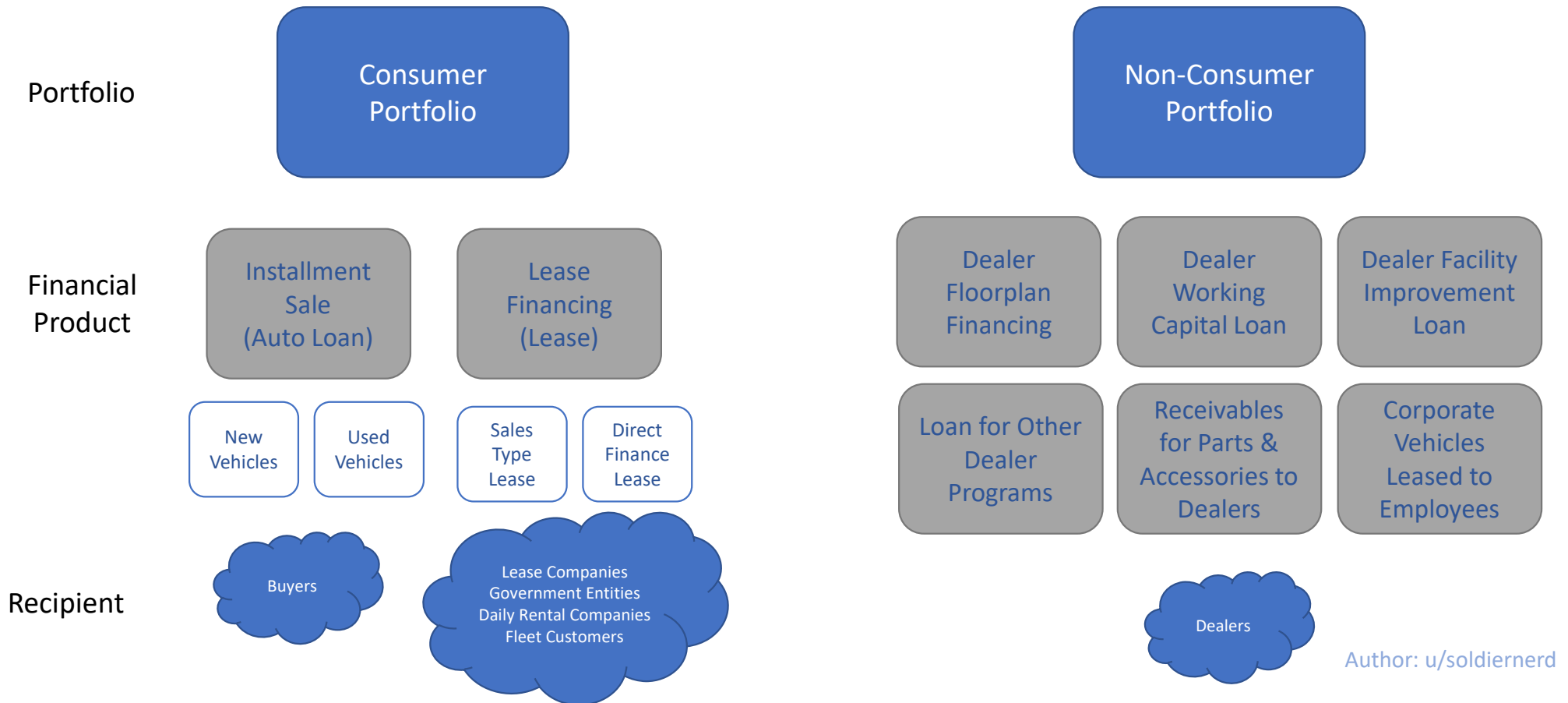
Automaker Financials

Case Study: Ford Credit

Author: [u/soldiernerd](#)

Ford Credit Portfolios

(Definitions on next slide)



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Terminology

- **Installment Sale:** This is a normal auto loan. Borrower owns the car once the loan is paid off.
- **Sales Type Lease:** Lessor recognizes some revenue at lease inception
- **Direct Finance Lease:** No revenue upfront, replace leased asset with receivable.
- For more on Sales Type vs Direct:
<https://tinyurl.com/yb4eemvk>
- **Floorplan Financing:** A loan to the dealer providing capital to buy inventory (wholesale vehicles) from the automaker in order to fill their dealership and sell to consumers

Overview

- Large Automakers have finance divisions which act sort of like central banks providing liquidity to the entire automotive life cycle
- Because they are involved in numerous complex financial operations, these finance divisions often carry large amounts of debt.
- This can shock the uninitiated investor who doesn't understand the nature of these operations. This presentation will attempt to assuage those fears by peeling back the curtain on some of the financial structures used by automaker credit operations.

Scenario

- Ford Motor Company manufactures vehicles, and wholesales them to dealerships.
- 25 cars at an average of \$35,000 = \$875,000.
- The dealer doesn't have this money, or doesn't want to lock it up in inventory, so they get a loan from Ford Credit to buy the cars:



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Scenario

- This is called a “[floorplan loan](#)”
- Dealers often also finance new construction of dealerships, site improvements, and some operating expenses
- These loans are collateralized by the inventory they purchase



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Scenario

- A consumer buys a car (for more than the wholesale price) with cash or financing.
- Financing may be through Ford Credit or another bank.
- The dealer must deliver the wholesaled amount to Ford Credit, and the floorplan loan balance is reduced proportionately.



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Scenario

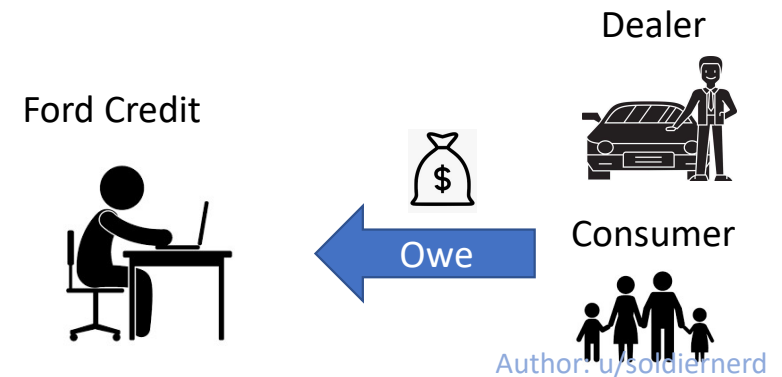
- If the vehicle is financed through Ford Credit, they will collect interest on it, in addition to recouping their capital, for the term of the loan.
- Many such transactions happen every day, resulting in Ford Credit lending billions of dollars a year to dealers and consumers alike.
- Leases are also handled by Ford Credit.



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Scenario

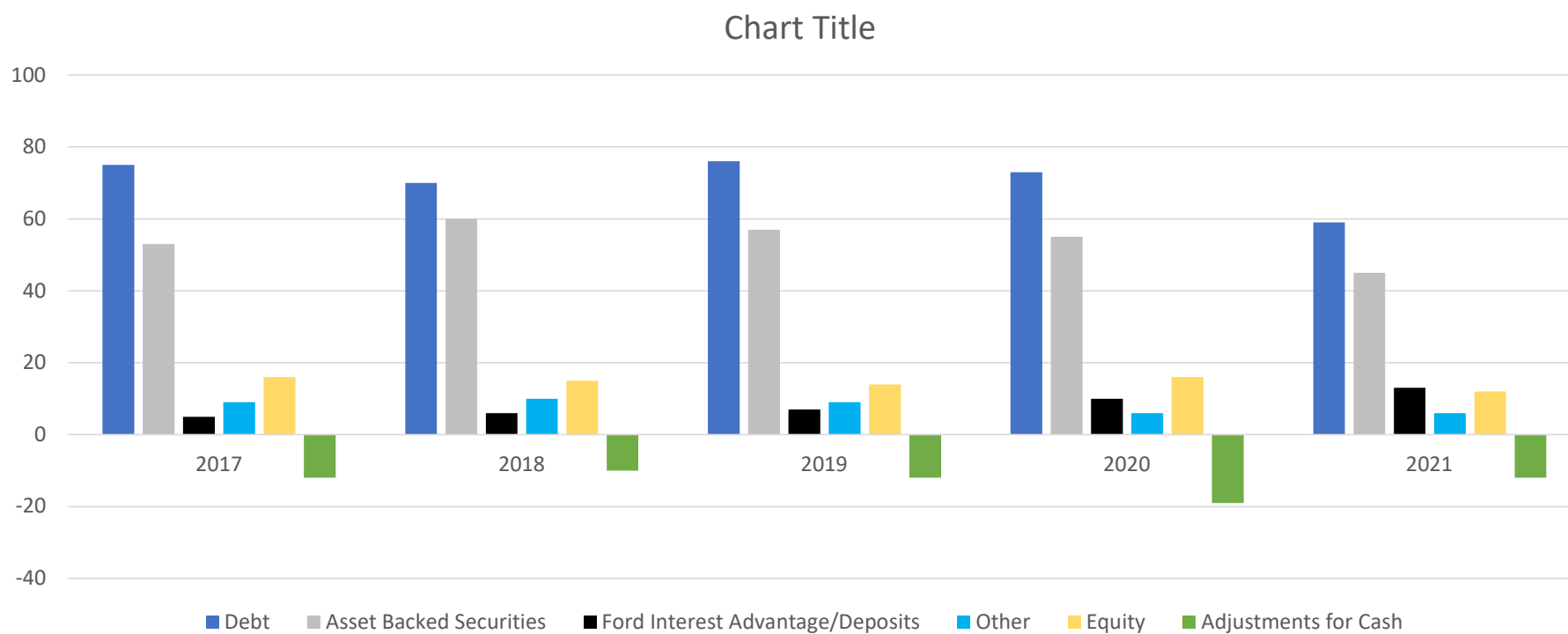
- These loans show up as **assets**, called “financial receivables” on the balance sheet.
- They are assets because they represent money that belongs to Ford Credit.



Assets

- One special type of financial receivable is the **Asset Backed Security**, or **ABS**.
- Ford Credit bundles tranches of dealer and auto loan into securities, and sells them to investors.
- Ford Credit creates a “**Variable Interest Entity**” or **VIE**, which holds the ABS and sponsors it on the market.
- When investors buy the ABS, Ford Credit, through the VIE, receives the cash.
- Investors don’t receive all the interest from the underlying loans. Ford Credit receives a cut of interest as well. This allows Ford Credit to offload default risk, receive some interest, and get their cash back before the loan matures.

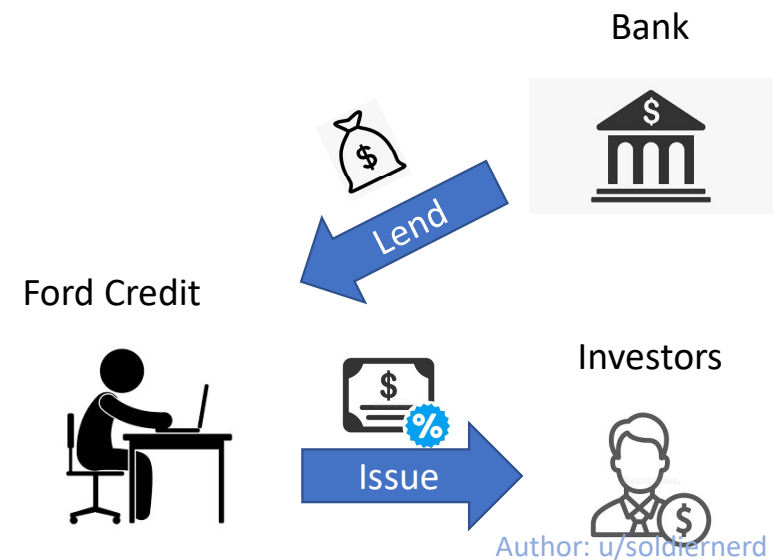
Ford Credit Receivables



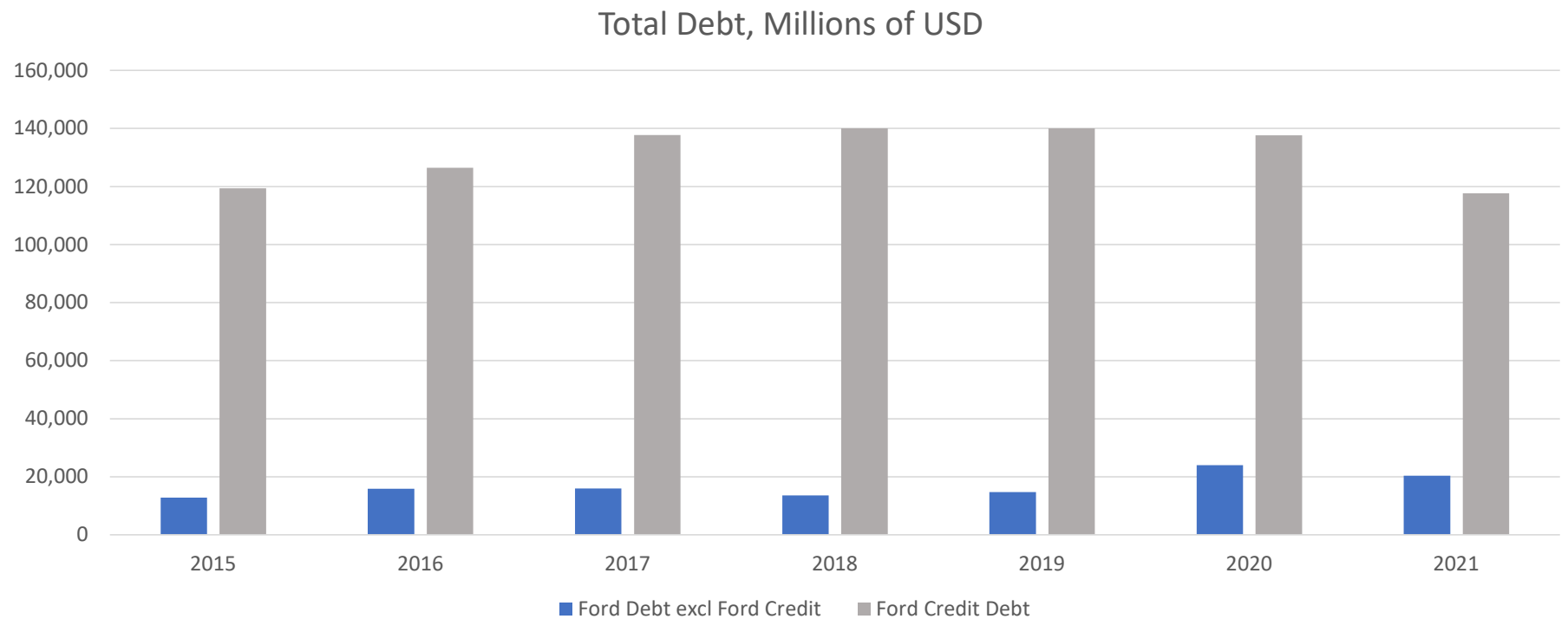
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Liabilities

- So where does Ford Credit get all the money to lend out?
- They borrow it!
 - Unsecured Debt
 - Selling Asset Backed Securities
 - Commercial Paper
 - Ford Interest Advantage
- These show up as **liabilities** on the balance sheet.
- This is money Ford Credit must repay.



Ford Debt



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Summary

- To summarize, Ford Credit acts as a central bank providing liquidity to the Automobile market.
- Ford Credit obtains liquidity by borrowing money at lower rates than the rates it will charge on loans.
- This is **debt** on the balance sheet.
- Ford Credit takes this money and loans it to dealers and consumers. These loans show up as **assets** on the balance sheet.
- Using Asset Backed Securities, Ford is able to offload much of the risk of default. If ICE vehicles experience rapid depreciation, the bulk of the loss will be borne by ABS investors, not by Ford Credit.