BHPH CAPITAL

By Peter A. Salinas

Gary Page, president of Small Dealers Assistance, based in Atlanta, Ga., probably said it best when it compared the buy here-pay here capital markets to airline travel. He said the rules for flying changed dramatically and forever after Sept. 11, 2001. He said the housing crisis and subsequent collapse of the credit market are akin to the changes in travel. The rules for getting money to fund your BHPH operation changed dramatically and for the foreseeable future.

Leedom Financial Services

Jim Garvin, COO of Leedom Financial Services, based in Sarasota, Fla., said there are essentially two forces at play in the buy here-pay here marketplace in terms of capital.

First would be the increasing demand for the product, and every single indicator shows that demand is on the rise. The second force is what is thaw in some of the capital markets, which means there is a slight ray of hope breaking over the horizon.

"We don't have full light and there's lots of darkness everywhere, but there is some light beginning to shine," Garvin said. "This is a metaphor for the fact the markets are still tight but loosening ever so slightly. The days of easily available capital for BHPH dealers are probably not going to return anytime soon."

Garvin believes capital will be showing up, slowly, but it won't be priced at the low points seen early in the last decade.

"Watching margins, advertising right, buying right continue to be critically important," Garvin said. "The dealers who do that, will be the biggest beneficiaries of that capital that does come back into our space. Our opinion is that 2010 will be a really good year for the business."

Small Dealers Assistance

Gary Page, president of Atlanta-based Small Dealers Assistance (SDA) Inc., said 2009 was a good year for his firm, though many dealers, especially those in areas of the country that were struggling, did not do well last year.

"We actually focused our business on areas of the country where the economy wasn't as hard it as others," Page said.

The ability to pick and choose which dealers and which areas of the country to do business, helped SDA to a very successful year, though Page wouldn't disclose the private firm's profits.

"The shakeout that occurred in our industry was swift and deep," Page said. "However, if you made it through everything we've been through and you are still standing, have a positive outlook, we want to speak with you."

Page noted that dealers who have lost a line of credit or had a local bank or other funding source curtail the amount of capital available to them have somewhat limited options.

He said dealers can either put the notes they have to work for them and put more money on the street to grow their portfolios, or they can sell fewer vehicles by requiring higher down payments.

Selling the notes outright can be problematic for most buy here-pay here dealers. Many companies that buy notes "cherry pick" a portfolio taking the best accounts, and basically deprive the dealer of the most lucrative portion of the business, the payments and interest from a well-performing finance contract. Many of these firms take over servicing the accounts, which alienates customers and limits a dealer's opportunity to develop the kind of relationship that results in repeat and referral business.

Page said SDA's program neither cherry picks and always gives the dealers the ability to collect directly from their customers.

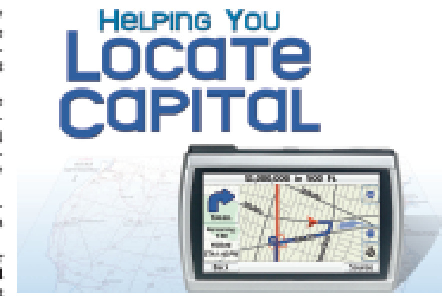
"When the capital markets dried up in late 2008, lines of credit evaporated, floor planning was cutback and dealers found their lifeboats had holes in them," Page said. "They had to look for more boats."

He said in 2008 dealers, whom he hadn't spoken with in 15 or 20 years began to call him up searching for cash to operate their business.

"While our opportunities were vast, we had to look at each individual dealer and each deal they way we always do," Page said. "In fact, we had to be more selective on who we chose to do business with. If you were well-capitalized and, been around a long time, you were in a good position."

Page said SDA had a 20 percent growth rate in 2009 and he anticipates a similar rate of growth for 2010.

"If you look at what happening in the BHPH industry you can see a situation where growth in this market will continue for at least the next 3-5 years," Page said. "Banks are still not doing much and we don't see them breaking loose any time soon. Hedge funds and other capital markets are still very cautious, and while some are looking around, keep in mind they dealers access money through the capital markets has changed permanently. Things will loosen up, but it will NEVER be like it was."



Page said he knows the rule about saying never, but feels confident that the ability to secure capital without a personal guarantee at pre-2008 advance rates, just isn't likely to occur again—ever.

So what's a dealer to do to secure cash from capital providers such as SDA.

Page said it's important for dealers to limit their leverage and have a rainy day fund. He wasn't specific as to the size of the fund, because it will be different with each dealership.

"You also need to operate lean and mean," he said. "Keep your overhead in check, watch the number of people you have working for you and focus on collections, collections, collections."

He said a focus on the fundamentals of Business 101 makes him stand up and take note of an operation.

"Listen anything that makes you more efficient and inspires you as a profession is good," he said. "Join a Twenty Group, attend a convention, get involved in a training program. We're looking for operators who know what this industry is all about. If we learn something new from you, all the better."

Page said the days of 70 percent advance on the dollar are gone, but notes they have competitive rates and that the SDA program continues to be an efficient way to raise capital without giving up control of the customer.

"It's much more cost-effective than selling off notes," Page said. "If you are a strong collector, and can keep an account paying, you are far ahead in this game. You get the repeat and referral business and you have the cash to keep rolling. You keep your eye on the ball, collect the cash and we'll help with the capital."

Page wouldn't be specific as to the number of dealers in the SAD program except to say "we have hundreds of dealers in 36 states." Among those 36 states are five where SDA has limited the including California, Florida, Michigan, South Carolina and Nevada.

"On the other side of that those areas that have high military concentrations are productive areas," Page said.

Page said he's seen the trade articles and heard from dealers that special finance is beginning to make a come back.

"Look, it will come back, but it will be modified tremendously," he said. "Think about my analogy to plane travel. You can still get on a plane, but you've got to do a lot more things before you get on. It will be true for the dealer and the consumer. It was the dealers who had 80 percent of their business as special fi and 20 percent BHPH, who completely switched their model and are now doing 80 percent BHPH that survived. They other guys aren't even around to talk to."

Car Financial

Rick Potter, president of Atlanta-based, CAR Financial said his business in supplying capital to by here-pay here dealers has been strong. While 2008, was good, he said 2009 was great.

He said the successful dealers who weathered the capital meltdown of 2008-2009 did so by returning to the "retrenched" buy here-pay here deal structure. He said dealers using the pre-2004 BHPH deal structure that properly accommodates consumer risk are doing well, and are those his firm is looking for.

"Many of the BHPH mega stores that abandoned this model in favor of expansion have failed or been financially damaged due to a lack of capital to support unrealistic growth expectations," Potter said.

"He said car financial is looking to buy deals that are in the 25-30 month range and have already been proven with six to eight months of successful payments," he said. "We're much more confident in buying a note where the dealers been watching his own money. We've developed a proprietary formula that looks at the vehicle make and model, age, balance, maturity and the original deal structure."

He said CAR Financial must not only be confident in the dealer's ability as an operator, but must be confident in the deal structure and the vehicle or the program simply won't work for them.

Potter said the days of "silly" money are gone. There simply isn't capital available for dealers to expect a 60-80 percent advance on the dollar, and that they should expect capital with terms of 40-55 percent advance rates.

He said one of the biggest problems facing dealers and CAR Financial as a capital providers is dealer's access to the right inventory at the right price.

"Dealers are having a harder time finding the vehicles that meet their model and our model," he said. "Special finance lenders need vehicles that fit their model, and they're available, but not at the right price. If the price isn't right, they can't issue bonds and are not able to securitize."

Dealers can jump the note from 25-26 months to 30 months or even 40, but then the vehicle won't last as long as the note, and CAR will not be able to work with that dealer.

"The other option is to increase the down payment, but then the dealer limits his volume," Potter said. "Also, it typically increases the default rate. You can't sacrifice good deal structure because the inventory is more expensive. Dealers have to think like a finance company."

CAR Financial has a variety of flexible programs to fit the needs of a wide cross-section of dealers. Dealers can remain in control of the account, or they can turn over collections to CAR.

Potter said as long as unemployment remains high, most BHPH dealers and subprime finance companies will see high delinquency and charge off rates. He said when you know the customer is out of work or trying to make partial payments, you have to be tough and go get the car. Working with the customer is paramount, but you have to be realistic when necessary.

Potter said he typically sees organic growth in his firm of 5-10 percent annually. In any given year, about 10 percent of his dealers will end their relationship with CAR, while the firm will sign up 15-20 percent new dealers.