The Next Financial Meltdown, the Auto Industry

It is not surprising, with the federal government takeover of two thirds of the American auto industry, that the Dodd-Frank financial overhaul process largely exempted the industry from Consumer Financial Protection Bureau oversight.

Tie this in with the growth of the number of new nonbank lenders rolling out personal loans and other types of financing geared toward subprime borrowers and you have a recipe for disaster. Like the auto industry such lenders face far less regulatory scrutiny than do big banks. As a result these nonbanks already are grabbing a larger share of the home loans reaching 37.5% as of 2014. They are offering subprime loans called 'nonprime loans' and require as much as 30 percent down to safeguard their investment.

Auto loans to people with tarnished credit have risen more than 130 percent in the five years since the immediate aftermath of the financial crisis, with roughly one in four new auto loans last year going to borrowers considered subprime, people with credit scores at or below 640.

The Wall Street Journal has reported that "borrowers who took out auto loans over the past year are missing payments at the highest level since the recession. More than 2.6% of car-loan borrowers who took out loans in the first quarter of last year had missed at least one monthly payment by November, the highest level of early loan trouble since 2008." More than 8.4% of borrowers with weak credit scores who took out loans in the first quarter of 2014 had missed payments by November, according to the Moody's analysis of Equifax credit-reporting data. That was the highest level since 2008

Low-interest rates and wider credit availability have helped propel the U.S. auto industry's comeback from the recession but as the industry lowers loan standards to continue selling cars the risks grow with another bubble in the making.

If wages rise and people get to buy new car, that's great. But if wages don't rise, what is actually achieved by making it easier for people to go into debt to buy them? It would seem that it all has to do with politics. The contribution to the U.S. GDP, from new and used motor vehicles and auto parts, has risen to 0.42 in the second quarter of 2014 driven by a robust post-recession auto-sector recovery fueled largely by cheap credit.

The administration's position as well as the industry is, as long as lenders and investors see that more than 96 percent of auto loans payments are current, there no incentive to curtail borrowing.

The bottom line is these nonbank financial institutions and the auto industry are loaning money to people who cannot afford the loans. When the borrowers cannot afford to pay those loans back it is going to set off an exploding chain reaction not only bring down these nonbanks but the auto industry itself. But it probably will not be on this administration's watch so who in this administration cares. At least they can claim that the economy is expanding under the Obama policies.