

The Impact of War and Recession on Vehicle Remarketing

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Many people are wondering what impact the current economic and political situation may have on new and used vehicle markets in the U.S. To gain some insight, it is worth reviewing what happened to these markets during the 1990-91 Gulf War and recession. Here is a brief timeline of national events during that period:

July 1990 - Economic contraction begins; previous expansion had lasted 92 months from November 1982-June 1990.

August 1990 - Iraq invades Kuwait; U.S. Operation Desert Shield begins primarily as a defensive measure.

November 1990 - U.S. President George H.W. Bush orders more U.S. troops to the Gulf for potential offensive action.

January 1991 - Operation Desert Storm begins.

February 1991 - Cease-fire takes place at midnight on February 28.

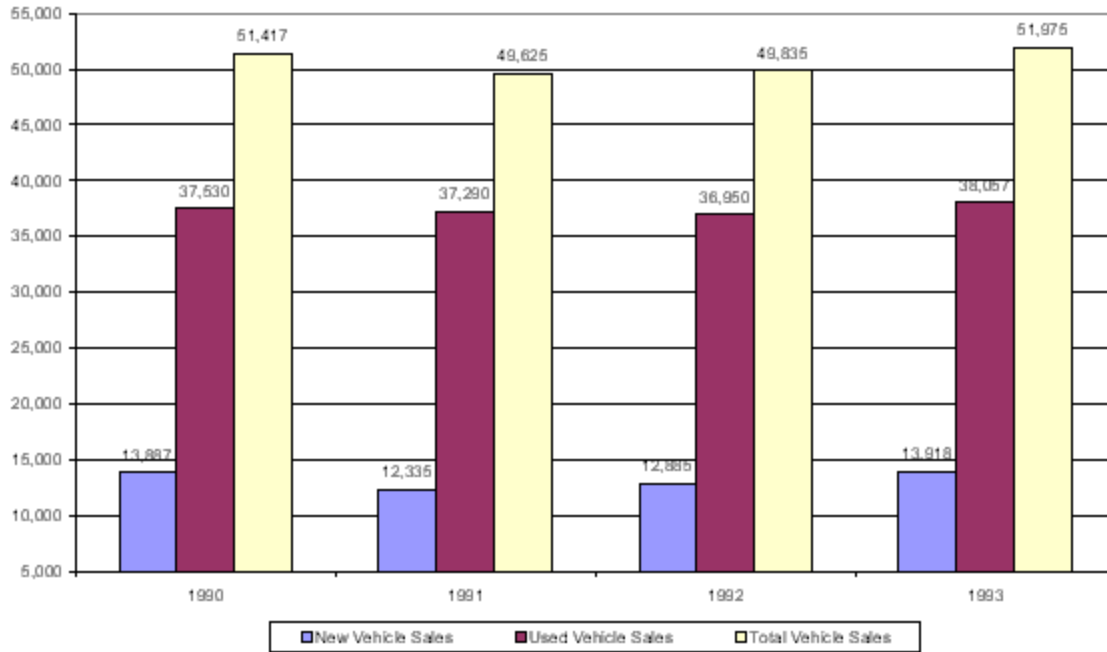
March 1991 - Economic contraction ends, first month of current expansion -- the longest ever -- begins.

November 1992 - GDP returns to the level achieved prior to the recession.

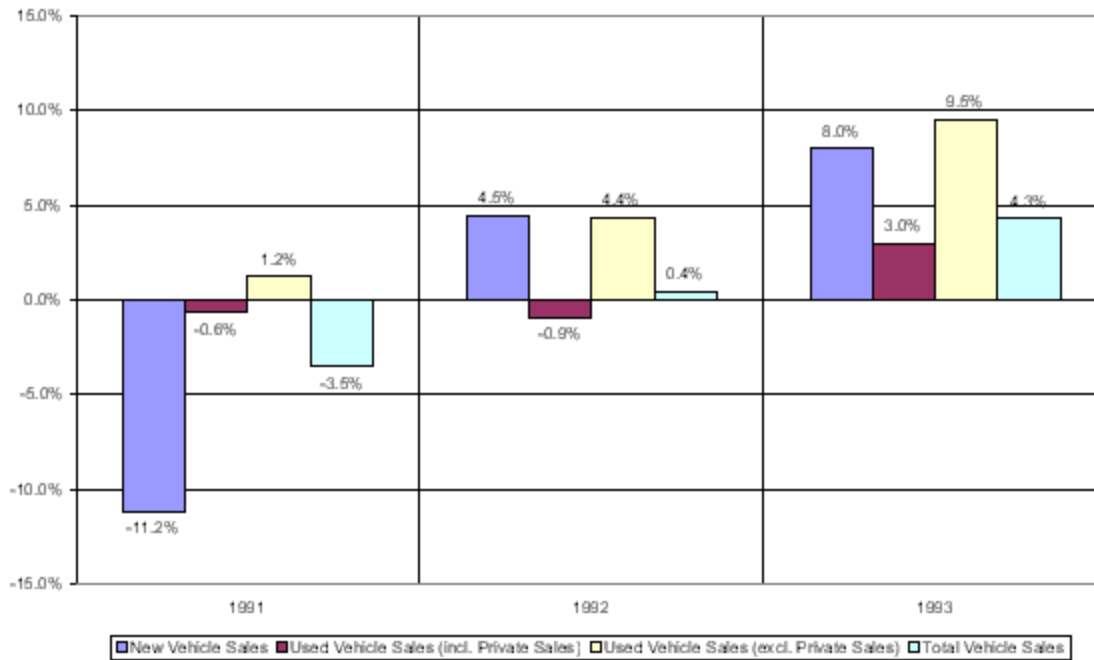
The above events seem uncannily like the current situation -- down to the name of our president! The U.S. is again faced with potential war and recession at the same time.

The following linked graphs show total annual new and used vehicle sales during and immediately after the Gulf War and coincident economic recession/recovery.

New and Used Vehicle Sales During Gulf War/Recession
(000s Units)



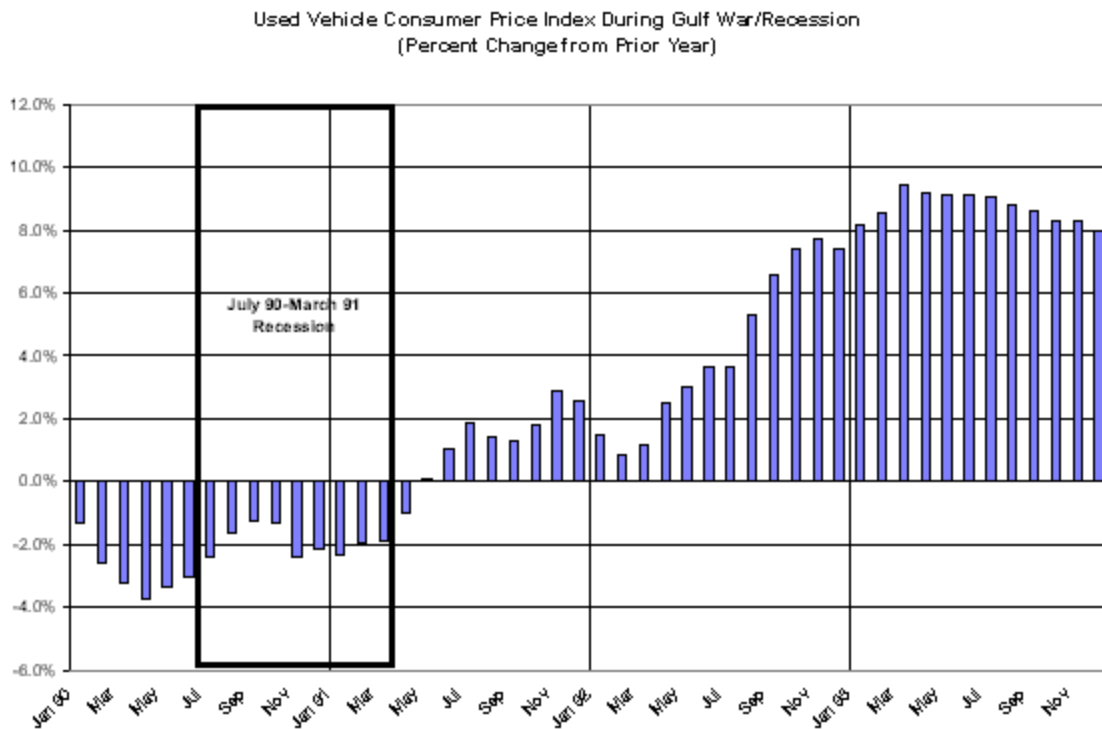
New and Used Vehicle Sales During Gulf War/Recession
(Percent Change from Prior Year)



Source: Automotive News Data Center, CNW Marketing/Research, and ADESA Industry Analysis.

The graphs show that new vehicle sales contracted significantly during 1991, rebounded modestly in 1992, and recovered to previous levels in 1993. Throughout that same period, total used vehicle sales were relatively constant, and, more importantly for the vehicle remarketing industry, used vehicle sales by dealers (i.e., excluding private used vehicle sales), actually increased. This may be due to private individuals holding on to their used vehicles, combined with increased demand for used vehicles, during times of economic uncertainty. This results in increased demand for, and sales of, used vehicles by franchised and independent dealers.

Also of concern to remarketers today is the question of what will happen to used vehicle prices, which will drive the values sellers can attain for their vehicles at auction. The following linked graph shows the performance of one measure of used vehicle prices during the Gulf War/Recession period.



Source: Bureau of Labor Statistics and ADESA Industry Analysis.

As the graph shows, used vehicle prices according to the Consumer Price Index were down throughout 1990 and did not begin rebounding until May 1991. Wholesale prices during that time frame mirrored these trends.

The Current Situation

Immediately prior to the deplorable events of September 11, many economists were predicting a recovery from the soft economic conditions of the first half of 2001. Encouraging signs included declining manufacturer inventories and increased factory purchase orders, supportive consumer spending levels, and government stimulus in the form of tax and interest rate cuts. The dramatic impact of the terrorist attacks on the airline industry, retail sales, and other sectors of the

economy would suggest that even the most optimistic of us would do well to hope for the best, but prepare for the worst.

Worsening economic conditions combined with the potential for war might lead to a similar scenario for new and used vehicle sales as that witnessed in 1990-91.

Already this year, we've seen evidence of a decline in new car sales offset by an increase in used car sales, as the following table shows.

New and Used Vehicle Sales
(000s of Units Sold)

	Year-to-Date thru August		Increase/(Decrease)	
	2001	2000	Amount	Percent
New Vehicle Sales	11,516	12,109	(593)	-4.9%
Used Vehicles Sales	29,180	28,565	615	2.2%
Total Vehicle Sales	40,696	40,674	22	0.1%

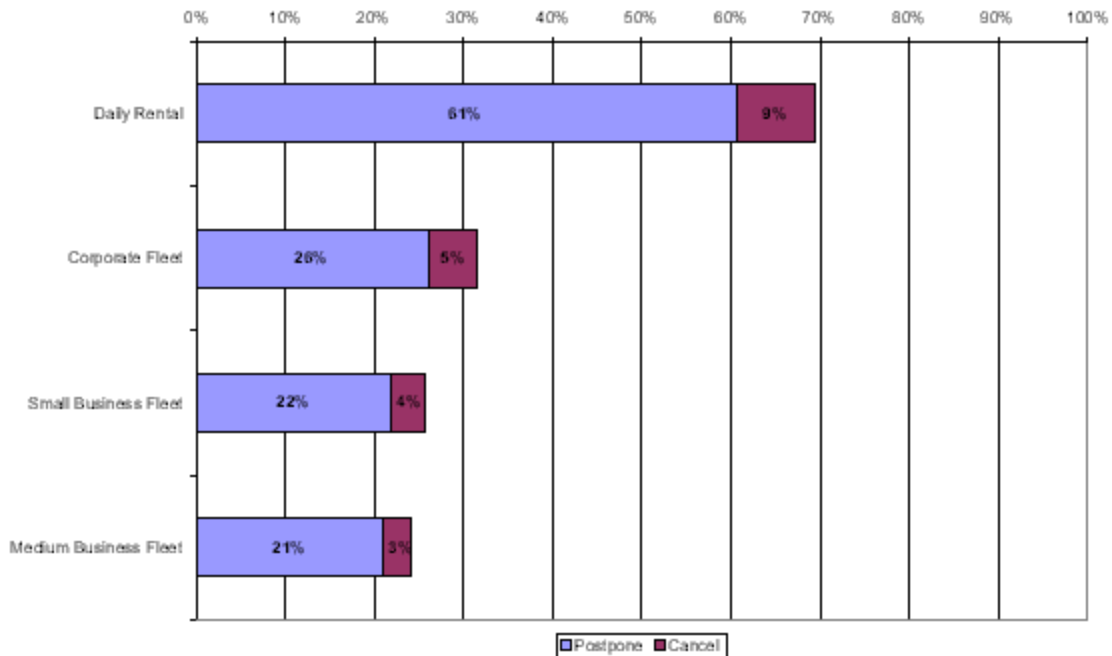
Source: Automotive News Data Center, CNW Marketing/Research, and ADESA Industry Analysis.

Under tough economic conditions, remarketers might expect dealers to actively attend auctions to obtain vehicles for customers wishing to purchase a used car, but to bid less aggressively for those vehicles. After back-to-back record new car sales years in 1999 and 2000, large numbers of vehicles will be returning for remarketing in the coming months. Coupled with the high new vehicle incentives and zero-percent finance packages now available to new vehicle buyers, the ample supply will be coming at a bad time for remarketers trying to sell these nearly new vehicles at prices approaching previously forecasted levels.

Another negative factor relative to wholesale prices is the potential for rental companies to downsize their fleets in the event of permanently lower demand for business and leisure travel. Typically, there is a seasonal surge in off-rental volume after Labor Day as mileage on rental units begins to exceed program parameters or prudent limits, and as the new model year begins. Expectations now are that this seasonal surge may be exceeded by as much as 60%. Moreover, many rental companies are, like the airlines, in dire financial straits. These troubled companies may return all their rental units to auctions at once.

Recent data suggests that rental companies and commercial fleet owners are also postponing or canceling new vehicle orders, as shown in the following linked chart.

Percent of Fleet Companies Planning to Postpone or Cancel New Vehicle Orders
Based on CNW Marketing/Research Survey



Source: CNW Marketing/Research and ADESA Industry Analysis.

This may mean that off-rental supply will diminish over time, although much of this perceived need to downsize may change as the country's perception towards travel changes.

Conclusions

The outlook for the auction industry is generally positive, as already healthy levels of off-lease units are reinforced by a surge of off-rental units. Consumer demand for used vehicles during recessionary times, and lower used vehicle supply from trade-ins as new vehicle sales drop, will draw dealers to auction for needed units.

Remarketers will surely be able to get their autos sold, but the "double-whammy" of high new vehicle incentives and high supply from past record new vehicle sales levels will worsen already soft wholesale prices. The residual value problem we were beginning to work past may be with us for several months to come.

The biggest winner of all may be the consumer, who will face an even better buyer's market than he or she does today. Great deals on new vehicles, late-model pre-owned certified, and older used vehicles allow consumers to purchase the best quality new and used vehicles ever available – at bargain prices. And even in tough economic conditions, these bargains may be too good to pass up.

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