Regulated Down Payment for Auto Loans: Limited Impact to Consumer Finance Industry

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PEFINDO views that the automotive financing industries will remain stable in medium term. The new regulations announced by Bank Indonesia (BI) and Badan Pengawas Pasar Modal-Lembaga Keuangan (Bapepam-LK) regarding minimum Down Payment (DP) for automotive loan will certainly affect the capability of the financing companies to book new financing in short term, as the demand in general will decline. However, in the longer term, the impact should be minimal as real demand for automotive products remain high and finance companies should be able to find new strategies to minimize the impact of lower financing volume as a result of increasing DP. In addition, in the long run, we expect this policy will also improve the companies' asset quality profile in line with increasing portion of high DP in their portfolio.

On 15 March 2012, BI issued Circular Letter No. 14/10/DPNP which among others regulates minimum DP for car financing for non-productive use at 30% and motorcycle financing at 25%. In the case of car financing for productive use, the minimum DP is 20%. Besides banks, finance companies must follow this regulation when providing financing under joint-financing (JF) scheme with banks. At the same time, Bapepam-LK as the regulator for consumer finance companies also issued Finance Minister Decree No. 43/PMK.010/2012 to cover disbursements funded by other schemes, such as debt securities issuance, direct bilateral or syndicated loans, or other funding sources. Under this decree, DP is set at a minimum of 25% for car financing for non-productive use, and 20% for car financing for productive use as well as motorcycle financing. Both BI and Bapepam-LK regulations have 3 months adjustment period and will be effective on 15 June 2012.

PEFINDO believes there will be an immediate effect after the regulations become effective, in the forms of lower new automotive financing particularly in second half of 2012. Currently more than 70% of automotive sales are done using credit scheme. In motorcycle financing segment, more than 60% of consumer financing companies' portfolio is using low DP (below 20%) scheme, while in car financing segment, the portion of low DP is substantially smaller. Finance companies accept low DP to enjoy higher financing amount and better margin, especially if the customers' credit risk profiles meet their preferred criteria. On the other side, there are customers with limited income generating capability which can only afford to buy vehicles under low DP scheme. Higher DP requirement may cause these customer segments to postpone or cancel their automotive purchase plan, considering they will need to have more funds for down payment. PEFINDO views these segments will be the main contributor of declining financing amount starting second half of 2012 while impact at the company level will depend on the magnitude of these segments in each company's portfolio.

Based on PEFINDO's review, at present low DP occurs more for new vehicles financing compared to the used ones. Finance companies may accept low DP to support boosting new vehicle sales imposed by automotive principals, especially if products or customers profiles are within their preferred credit risk criteria. From a different angle, portion of low DP is generally higher in motorcycle financing than car financing, in consideration of lower income generating capability of most of motorcycle buyers. Based on our assessment, customers can purchase new motorcycles with DP as low as 10% or even less. Accordingly, PEFINDO views that although the new DP regime will affect all segments due to lower number of potential customers capable of paying the required DP, consumer financing companies focusing on new motorcycle should be affected the most, as the percentage gap to fill is considerably wider than other segments.

Despite the adverse impact of these regulations to the financing amount, PEFINDO also views that automotive and consumer financing sectors have proven their resiliencies during various economic downturns, including 100% fuel price hike in 2005 and tight liquidity in banking sector in 2008 – 2009. To minimize impact of low demand after the new DP regime in 2H2012, some finance companies will intensify their financing activities in 2Q2012. Risk profile of the existing financing portfolio already booked by the companies will not be affected under the new DP regime and remain at a manageable level to generate cash flow for fulfilling their outstanding liabilities. Sound financial profiles as well as synergy and support from parent companies will provide strong cushions to withstand impact of the plunge in financing volume. To some extent, higher DP required for banks (30% for 4-wheels & 25% for 2-wheels) may also create potential customer shifting to finance companies, as they require slightly lower DP (25% for 4-wheels and 20% for 2-wheels). In the long run, PEFINDO believes that companies that can cope with the firmer DP will harvest the benefit reflected by a stronger credit risk profile in their financing portfolio. Demand for automotive products will also eventually recover as there is still huge need for decent means for transportation which cannot be fulfilled by the existing public transportation in a medium term. Improving purchasing power of the consumers will also strengthen their saving capability and thus delay in purchasing new vehicles can be expedited. Automakers and consumer finance companies will also make their best effort to offset further decline in auto sales and financing volume by implementing new business and marketing strategies and still within the corridor of regulation. Those factors can mitigate negative impact created by the new regulations.

Despite our view on limited impact of the new regulation to consumer financing industry risk profile in overall, PEFINDO will closely monitor further development within the automotive and consumer financing sectors, particularly consumer financing companies within PEFINDO's portfolio. We believe impact to each consumer financing company will be different depending on their business characteristics, and necessary rating action will be taken if we believe that the impact may substantially weaken the companies' credit risk profiles.