GM puts leasing on a short leash

DAVID BOOTH

It seemed a little confusing. It certainly was dramatic. Was General Motors actually thinking of getting out of leasing? Or was it simply backing away from the lease subsidization that has been such a large part of The General's success? Was this one more in a long line of straws that would break the proverbial camel's back?

The real reason most of us were left confused by GM Canada's announcement was the total shock. Leasing commands a much larger portion of automotive sales north of the 49th Parallel than it does in the United States. We Canadians, with less disposable income than our American compatriots but no less inclined to drive beyond our budgets, lease a much higher percentage of vehicles with as many as 45% of new vehicles leased.

So, for the record, GM Canada is NOT getting out of the leasing business. It will simply stop subsidizing its leasing deals. Nonetheless, that GM would futz with one of its main sales tools seemed shocking. But not illogical.

The problems for General Motors are manifold. For one, as has been widely reported, the company is facing a possible shortage of cash. Though America's largest automaker has not yet run out of greenbacks, some analysts are predicting that exact eventuality within the next 24 months.

What has really exacerbated that problem is how dramatically the floor has dropped out of the truck and large SUV markets. And while it's immediately obvious how this might affect the selling price of a new vehicle in the showroom, its effect on resale values (and, therefore, on lease residuals) is even more dramatic. According to Dennis DesRosiers, "Residual value losses on four-year-old large pickups are currently 17.7% of their original manufacturer's suggested retail price and with large SUVs the residual losses are in the 10% of the original MSRP range."

Simply put, the residual values of all those trucks and sport-utes coming off lease have dropped steeply below what GM anticipated. Its leasing arm, once General Motors' money-lending cash cow, lost US$2.5-billion in the second quarter of this year.

GM may also have had no choice in its decisions. It only owns 49% of its eponymous financing arm. GMAC's majority stakeholder is Cerberus Capital Management, the private equity firm that recently bought Chrysler. Chrysler, too, is facing financial strain, so Cerberus is probably not feeling too happy about subventing money-losing leases. One has to wonder if Cerberus would have preferred to get GMAC completely out of the leasing business.

Indeed, in the United States, General Motors took pains to announce that it's business as usual, for the time being. In an e-mail obtained by the Associated Press, GM told dealers it will continue to offer leasing incentives, at least through August. "Obviously, current financial pressures will continue to affect our perspective on leasing," says Mark LaNeve, GM's North American sales chief. "That said, while we obviously can't make guarantees, we are in the market today with competitive programs to make GMAC leasing more affordable and plan on continuing to offer this financing alternative as part of our August incentive play on '08 and '09 models (with some adjustments and exceptions)." An industry insider suggests that those exceptions will be the volatile truck and SUV segments.

No doubt there will be alternatives to GM's leasing. GM Canada is already promoting extended-length, low-interest loans it claims can match or better monthly lease payments. What makes financing, even at low interest rates, more attractive than leasing to GM is that it shifts the burden of low residual values from the company's bottom line to the consumer's wallet (if your car plummets in value, you're stuck with the loss rather than the leasing company).

It will also be a boon to independent lessors. Lease Busters Inc., which bills itself as Canada's leading vehicle lease takeover facilitator, is already making hay with GM's announcement, saying it will "fill the gap" left by GMAC of Canada's decision to stop subsidizing leases.

According to Jim Matthews, general manager and owner of Lease Busters, "With GMAC Canada's Financial Services division no longer subsidizing lease rates, Lease Busters becomes the obvious alternative for drivers who, for personal or professional reasons, prefer to lease their vehicles." This even though the company currently finances only used vehicles.

Ironically, it is Matthews who seems the most upbeat about General Motors' prospects, saying he sees GM Canada returning to subsidized leases "in a three-to-six-month time frame" when all of the financial volatility south of the border calms down.

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dbooth@nationalpost.com

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While GM appears to be backing away from leasing in Canada, its U.S. wing plans to promote leasing with incentives.