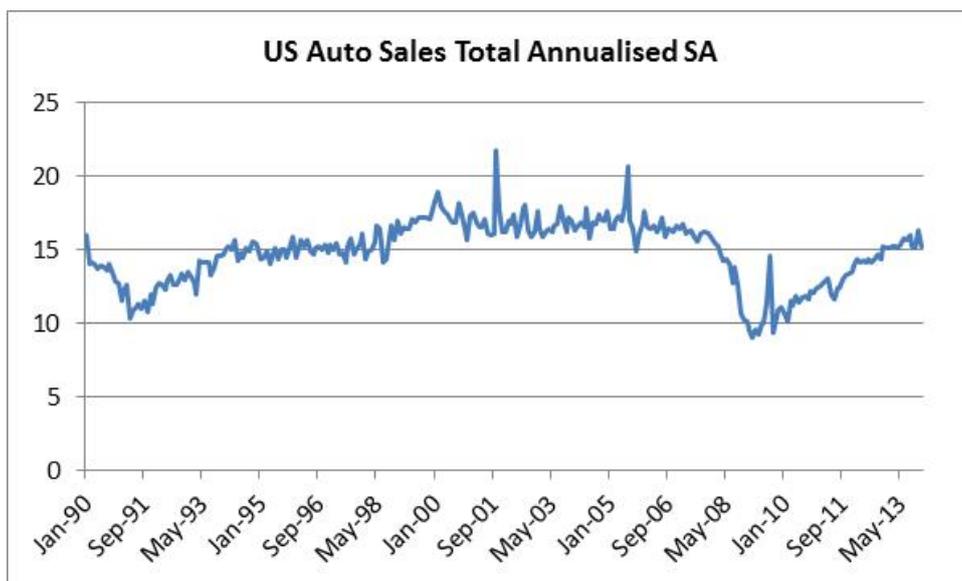


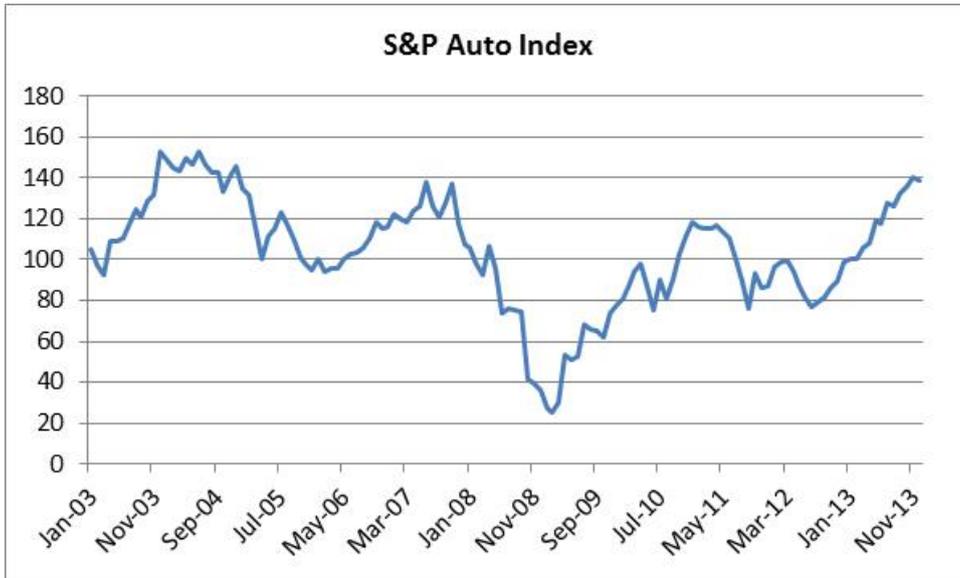
THE US AUTO MARKET



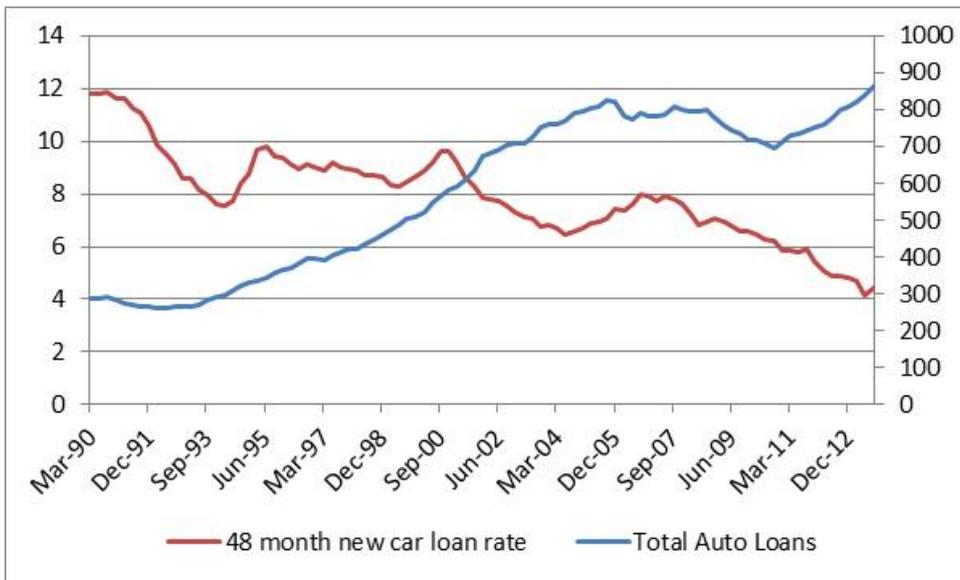
The US auto market has staged a very impressive recovery from the financial crisis.



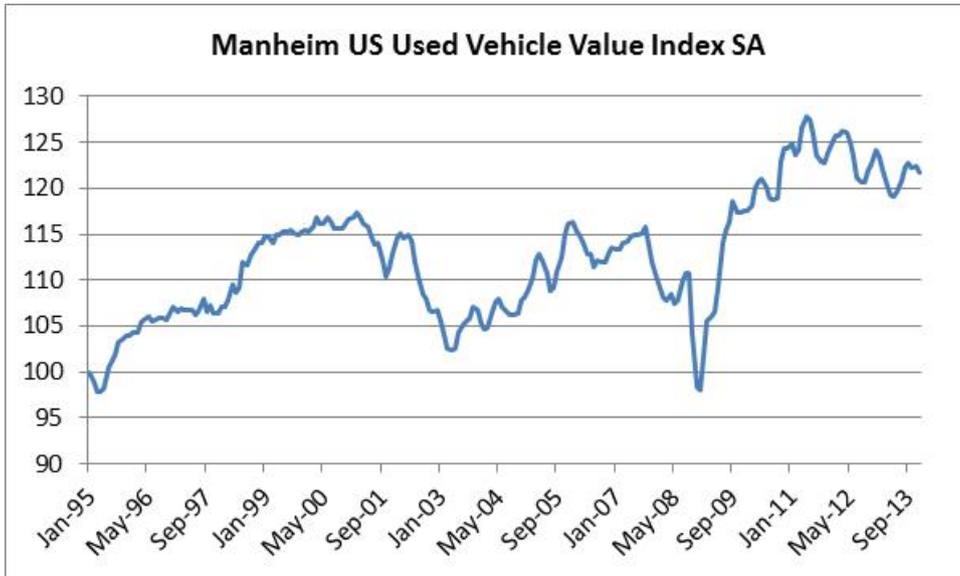
For investors that had the courage to buy at the lows of the financial crisis, they have been rewarded very well. The Auto index also returned 40% last year, outperforming the S&P in a very strong year for equities.



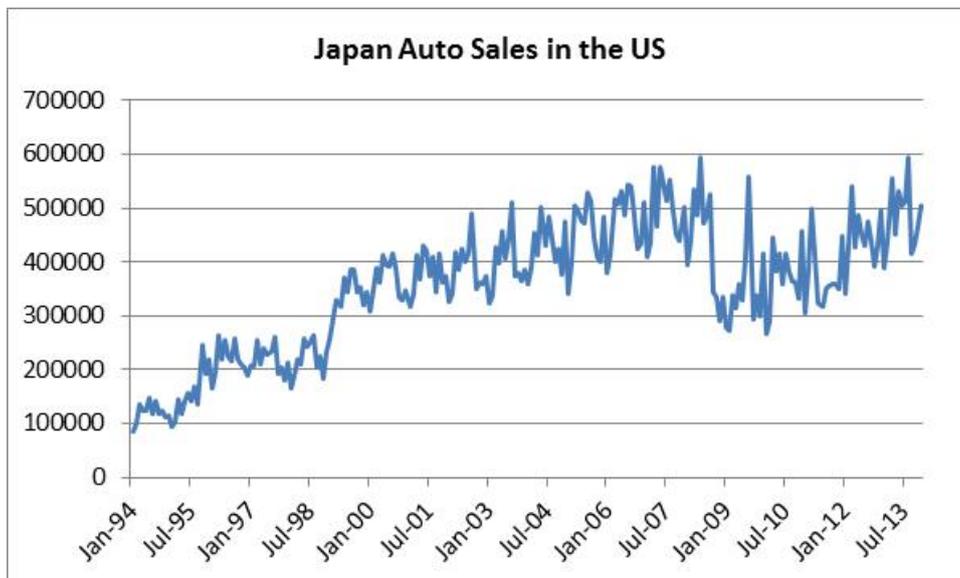
Autos, like housing, are a durable good that is generally purchased on credit. According to Fed Reserve data, recent car buyers in the US have benefited from very low interest rates on car loans. Lower rates have clearly stimulated loan demand.



After the financial crisis there was a reduction in supply of auto loans. This meant that would be new car buyers purchased used cars, which led to a large increase in the price of used cars. This can be seen in the performance of the Manheim US Used Vehicle Value Index.



One feature of the US Auto market is its openness to foreign competition, particularly Japanese auto production.



According to the most recent auto sales figures, imports make up around one third of car sales in the US. Japanese car makers have historically relied on US market for their profit growth as their domestic market has both fierce competition and stagnant sales.



Comparing the performance of the US auto sector to the trade weighted value of the yen seems to imply that US auto makers do relatively well when the yen is strong, such as the early 90's and again after the financial crisis. Periods of yen weakness such as from 2000 to 2008 are associated with relative underperformance of the US auto sector.

For me, many of the tail winds for the US auto sector seemed to have turned to head winds. Interest rates have risen recently, yen has weakened and the value of used cars in the states has begun to fall. The probability that US auto makers underperform the US market seems very high in my view.

INFORMATION

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 Source: Bloomberg, unless otherwise stated
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