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Market Report

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Automotive Insights from Kelley Blue Book

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NEW-CAR MARKET ANALYSIS:

Analysts Cautiously Optimistic on Future Vehicle Sales

- Alec Gutierrez, senior market analyst, automotive insights, Kelley Blue Book

Sales are on pace for the third consecutive year of double-digit gains and this certainly is reason enough to be optimistic. Aiding sales are positive developments in both consumer debt service ratios and auto loan delinquency rates, which have been in steady decline for the past 6 to 12 months. Vehicles are 10.8-years-old on average according to Polk, prompting consumers to seek replacement vehicles.¹ Although demand for new cars appears stable, uncertainty remains surrounding the future of auto sales.

IF ECONOMIC GROWTH CONTINUES AT ITS CURRENT PACE, WE EXPECT VEHICLE SALES TO REACH, BUT NOT SIGNIFICANTLY SURPASS, 15 MILLION UNITS BY 2014. KELLEY BLUE BOOK DOES NOT EXPECT SALES TO APPROACH 16 MILLION UNITS UNTIL THE UNEMPLOYMENT RATE IS NEAR 6 PERCENT.

- ALEC GUTIERREZ

According to some of the industry's top forecasters, light-vehicle sales in the United States will continue to grow, but the debate lies in by how much and how soon. There is a general consensus that sales in 2012 will be 14 to 14.5 million, slightly below the lofty expectations set after the first three months of the year. Beyond 2012, industry forecasts vary. By 2015, sales projections range anywhere between 15 to 17 million units overall depending on the strength of the economy at that time.

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Kelley Blue Book's latest forecast puts industry sales at 14.2 million units this year and anywhere from 14.5 to 15.0 million units in 2013. If employment growth and consumer confidence can get back on track, sales of 15 million units certainly are within reach. However, if unemployment remains above 8 percent and the economy continues to grow at a 1.5 to 2 percent growth rate, sales may level off and only moderately improve during 2013 and beyond.

If economic growth continues at its current pace, we expect vehicle sales to reach, but not significantly surpass, 15 million units by 2014. Kelley Blue Book does not expect sales to approach 16 million units until the unemployment rate is near 6 percent; a level that even the Federal Reserve believes will be a stretch by 2014. Unemployment is expected to be 7 to 7.7 percent by 2014 according to the Federal Reserve's June projection, putting a damper on hopes of a return to 16 million unit sales or more by that time.

Another concern is the question of interest rates. There is little doubt that the auto sales recovery has been largely driven by improved credit availability and near zero-percent financing. Interest rates cannot stay at zero forever, and although the Federal Reserve has pledged to keep rates at current levels through 2014, rates will likely increase at some point beyond that date. When rates start to rise, auto sales will pull back, tempering any momentum in industry sales growth.

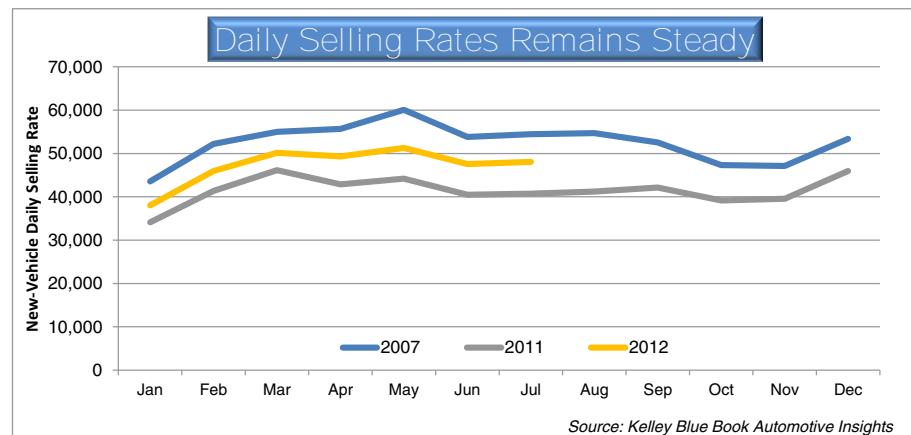
The analyst community recognizes the limitations weak economic growth can place on industry sales volume and with unemployment, consumer confidence and GDP all disappointing, an expedient return to 16 million sales is far from guaranteed.

¹ R.L. Polk & Co. News, January 17, 2012

New-Vehicle Demand Has Consumers Considering 'Affordable' Vehicles

If July is any indication of what to expect throughout the rest of the year and beyond, demand for new vehicles will continue to grow at a sluggish pace. Informed consumers, still weary of an uncertain economic future, will continue to seek practical and affordable models as they look to upgrade their current vehicle. With this in mind, dealers should focus on promoting vehicles that offer consumers the most value for the money.

New-vehicle sales continued to show solid annual gains despite unfavorable economic news through the end of July showing only slight improvements. The daily selling rate was flat month-over-month, but a healthy 17.9 percent above the July 2011 pace, when short inventory conditions hampered overall sales. Pent-up demand will remain a driving force in the near term and with supply conditions still favorable (there were 2.7 million new vehicles available for sale nationwide as of July 1; significantly better than the 2.2 million vehicles available in July 2011), existing stocks should be sufficient to satisfy demand.

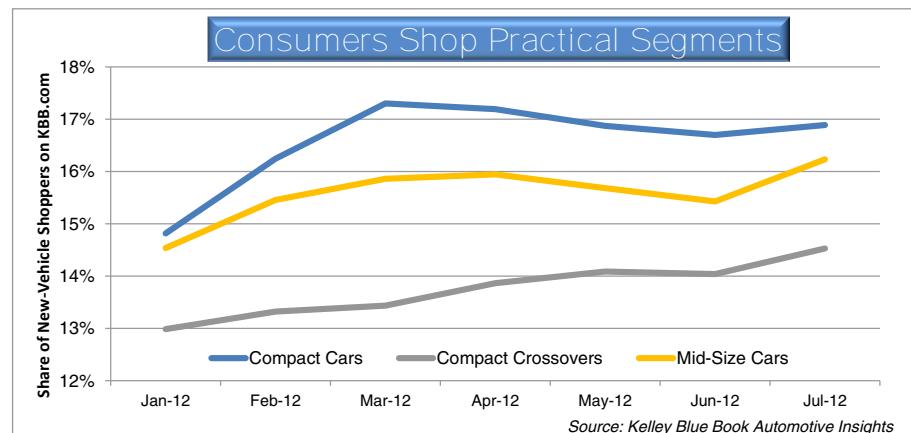


Mid-Size Cars, Compact Cars and Compact Crossovers Lead Consumer Interest and Sales

Sales of mid-size cars, compact cars and compact crossovers continued to lead the market in July, accounting for nearly 45 percent of all vehicles sold during the month. These vehicles have resonated well with shoppers in need of affordable transportation offering top-notch fuel economy without sacrificing amenities. Low finance annual percentage rates (APRs), cheap lease deals and cash incentive offers on soon-to-be redesigned models have been especially effective at capturing the attention of the buying public.

The mid-size category is in the midst of a banner year, thanks in large part to the remarkable annual increase in sales of the Chrysler 200, Ford Fusion and Nissan Altima, all of which have been popular due to generous cash support. Sales of the Chrysler 200 are up nearly 90 percent year-over-year through the first seven months of the year. In fact, the 200 has far surpassed sales of the Sebring it replaced, currently outselling Sebring's calendar year 2007 volume by more than 40 percent. The Fusion and Altima are up approximately 20 percent year over through July, surpassing the industry average increase of 14 percent. Each of these models has been available with upwards of \$3,000 in cash rebates throughout much of this year and as consumers have kept affordability a priority, these vehicles have thrived.

Redesigns also played a significant role in the mid-size category, as demonstrated by the segment-leading Toyota Camry with its 40 percent year-over-year improvement through the first seven months of 2012. In fact, the mid-size category is one of the few segments currently on track to surpass its sales volume figures of 2007, which was the last



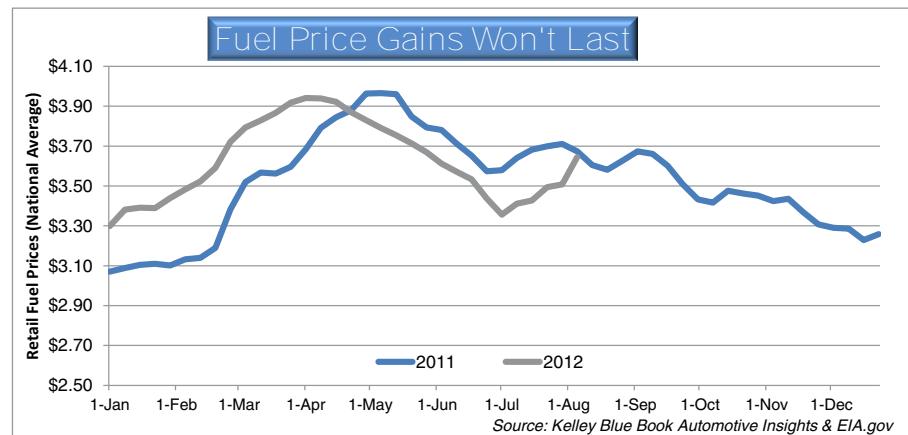
'normal' year of sales prior to the downturn. In July, KBB.com new-car site traffic jumped in the mid-size category, largely due to the introduction of the 2013 Nissan Altima.

Sales of compact crossovers also are surpassing 2007 volume levels as consumers have downsized from fuel-thirsty SUVs. This segment has grown tremendously since 2007 in terms of segment participants and market share. Compact crossovers also are one of the fastest-growing segments for new-car shopper activity on KBB.com, gaining a full 1.5 points of market share from January through July. Although typically more expensive than compact or mid-size cars, they offer tremendous value to small families in need of more cargo capacity without sacrificing fuel efficiency.

Compact cars remain the top-shopped segment on KBB.com, due to their low cost of entry and the slew of fresh redesigns currently available for sale. The Hyundai Elantra, Volkswagen Jetta, Ford Focus, Chevrolet Cruze and Honda Civic all were redesigned in the past year, helping to keep the segment at the top of consumers' minds. Compact cars accounted for 14.2 percent of all vehicles sold in July, and we expect consumer interest to remain high as shoppers seek affordable replacement vehicles.

Fuel Decline on Horizon

Although fuel prices recently have been on the rise, Kelley Blue Book projects cheaper gas ahead, perhaps below \$3.25 per gallon by year-end. U.S. crude inventories remain near a 20-year high, while fuel consumption steadily declined in recent years. With the poor outlook for job growth and grim economy, fuel consumption will remain depressed, which should help to keep gas prices in check through 2013. In fact, the Energy Information Administration (EIA) projected that gas prices will average \$3.28 per gallon nationally in 2013, well below the \$3.49 per gallon average expected for 2012. Although fuel prices are expected to ease, we believe demand for fuel-efficient vehicles will remain steady as budget-conscious consumers place a high priority on affordable vehicle purchases.

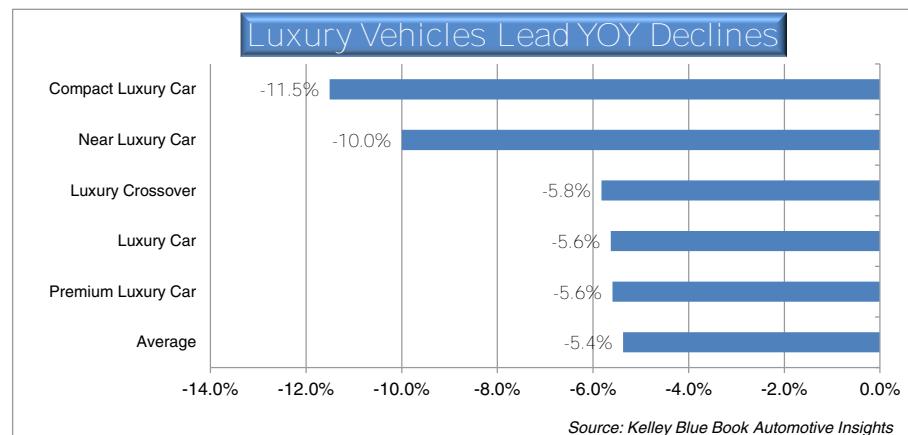


USED-CAR MARKET ANALYSIS:

Buyers Opting for Fully Loaded Standard Sedans, Instead of Luxury Counterparts

Luxury vehicles have suffered at auction as consumers have been less willing to pay premium prices for a used vehicle as values drop 7 to 10 percent from one year ago, surpassing the average industry decline of 5.4 percent. While values have been sliding, luxury vehicles have underperformed the market by a significant margin due to their high price point. Further driving down values of used luxury vehicles are the attractive finance and lease offers currently available on many new high-volume luxury vehicles. BMW currently is offering the 328i coupe for \$359 month on a 36-month lease, while Mercedes-Benz is running a similar promotion for the C-Class at \$369 per month on a 24-month lease.

In addition to competitive new-vehicle pricing swaying luxury buyers, the improved quality and amenities offered in most mainstream vehicles also are motivating buyers away from the entry-level luxury segment. Consumers today may be inclined to consider a loaded Hyundai Sonata or Toyota Camry rather than an Audi A4 or BMW 3-Series due to the more attractive price point and comparable feature set. With economic growth still stagnant and unemployment stuck above 8 percent, we likely will find more and more buyers opting to purchase fully loaded standard sedans versus their premium-priced luxury counterparts.



LUXURY VEHICLES HAVE UNDERPERFORMED THE MARKET BY A SIGNIFICANT MARGIN DUE TO THEIR HIGH PRICE POINT. FURTHER DRIVING DOWN VALUES OF USED LUXURY VEHICLES ARE THE ATTRACTIVE FINANCE AND LEASE OFFERS CURRENTLY AVAILABLE ON MANY NEW HIGH-VOLUME LUXURY VEHICLES.

-ALEC GUTIERREZ

Weak Travel Season Provides High Rental Car Volume and Inventory Relief at Auction

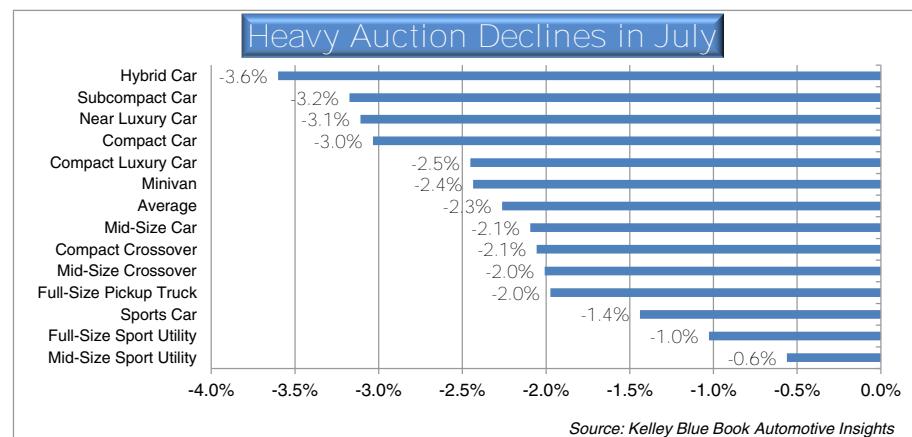
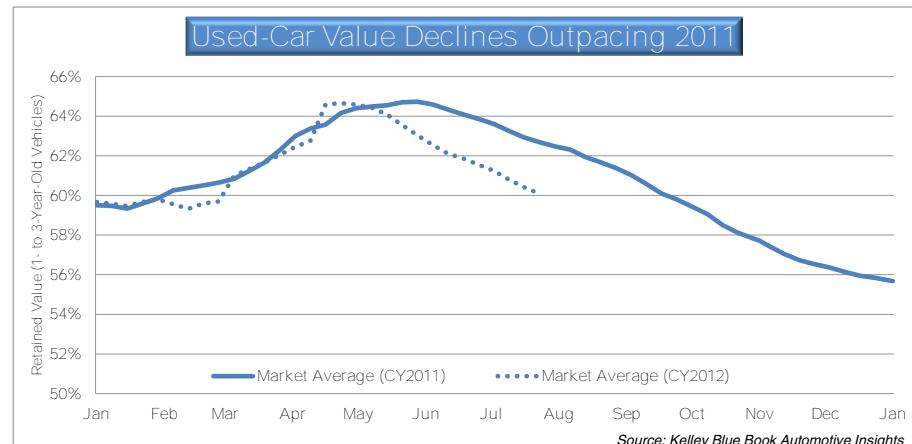
Lease returns remain light and will not increase until Q1 2013; however, dealers have seen some relief from earlier-than-expected high rental car volume at auction due to a weak travel season. With the economy improving at an anemic pace, consumers are travelling less often and for shorter trips. This has had a direct impact on the rental car business, reducing demand for rental cars and prompting rental car agencies to trim their fleets. This has helped to increase inventory at auctions, putting additional downward pressure on prices.

Franchised new-car dealers also have seen a jump in trade volume related to increased new-vehicle sales, but this has not trickled down to auctions since most dealers are retaining their trades for retail sale. Although dealers have seen some relief at auctions from higher rental car volume, they are unable to get enough inventory to fully stock their used-car lots. Most dealers we have spoken with have indicated that they are typically opting to retain a customer's trade-in rather than send it to auction. With inventory levels of both new and used vehicles better than at this time last year, but below historical standards, values of 1- to 3-year-old used vehicles are now down 5.4 percent from July 2011. At the start of July, values were down more than 4 percent year-over-year.

Used-car values tumbled 2.3 percent in July and are down more than 5 percent since peaking in May. These widespread declines are across all segments, with the most significant drops hitting fuel-efficient subcompact, compact and hybrid car values, which declined in consumer consideration with the drop in fuel prices. In addition to cheaper gas prices, wholesale values at auction have dipped due to improving, albeit still tight, inventory conditions and weak demand from consumers.

Further suppressing used-car values at auction are drops in demand for used vehicles due to comparable new vehicle and late-model used-vehicle pricing. On average, a 2012 model-year new car sells for 95 percent of original manufacturer's suggested retail price (MSRP), only marginally more expensive than the 85 percent of MSRP commanded by 1-year-old used vehicles. The gap between new- and used-vehicle prices is even tighter after factoring in typically lower finance rates and incentives on new vehicles.

We expect used-vehicle values to continue to decline in the months ahead.



USED-CAR VALUES TUMBLED 2.3 PERCENT IN JULY AND ARE DOWN MORE THAN 5 PERCENT SINCE PEAKING IN MAY. THESE WIDESPREAD DECLINES ARE ACROSS ALL SEGMENTS, WITH THE MOST SIGNIFICANT DROPS HITTING FUEL-EFFICIENT SUBCOMPACT, COMPACT AND HYBRID CAR VALUES.

- ALEC GUTIERREZ

Despite Declines, Used Fuel Sippers Remain Top-of-Mind According to KBB.com Site Visitors

Although we expect values to soften through the rest of the year, dealers can rest assured that there are a handful of segments consumers are actively shopping on KBB.com. Dealers planning to buy vehicles at auction should pay particular attention to mid-size cars and compact crossovers, since each of these segments have steadily increased in shopper activity from visitors to KBB.com.

Since January, share of used-car shoppers has jumped for the compact crossover segment from 5 to 5.5 percent. Although a relatively mild overall increase, it is noteworthy since many other competing high-volume segments have trended downward or remain flat. Share of KBB.com site visitors viewing mid-size cars has increased from 15.9 percent to 16.1 percent since January, a relatively mild increase but still worth noting. Consumers remain highly interested in compact cars with 17.8 percent of all used-vehicle intenders shopping the segment in July. Although compact car interest is higher than both compact crossovers and mid-size cars, interest is trending downward since fuel prices peaked.

To assist dealers looking for inventory in August, we highlighted 10 3-year-old vehicles available at a considerable discount from original MSRP. Since these are among the most affordable models in their respective segments, values should be relatively steady in the months ahead, even as the overall industry is expected to decline.

Dealers should remain cautious in the short term and avoid paying premium prices for fuel-efficient vehicles. Although values may increase slightly in the short term, if fuel prices continue to rise, the increase only will be short-lived. The current run-up in fuel prices likely will run its course as summer winds down and we expect fuel prices to continue to trend downward, along with values of fuel-efficient vehicles. Consumers will continue to seek fuel-efficient vehicles; however, they will not pay a premium, especially with so many new fuel-efficient vehicles available with lease payments below \$200 per month.

DEALERS PLANNING TO BUY VEHICLES AT AUCTION SHOULD PAY PARTICULAR ATTENTION TO MID-SIZE CARS AND COMPACT CROSSOVERS, SINCE EACH OF THESE SEGMENTS HAVE STEADILY INCREASED IN SHOPPER ACTIVITY FROM VISITORS TO KBB.COM.

- ALEC GUTIERREZ

10 Affordable Alternatives at Auction

Segment	Make	Model	VehicleName	MY	MSRP	Auction	Retention
Compact Crossover	Suzuki	Grand Vitara	Sport Utility 4D	2009	\$20,649	\$9,325	45.2%
Compact Crossover	Mitsubishi	Outlander	ES Sport Utility 4D	2009	\$22,325	\$10,900	48.8%
Mid-Size Car	Volkswagen	Passat	Komfort Sedan 4D	2009	\$28,990	\$14,275	49.2%
Mid-Size Car	Mazda	MAZDA6	i Sport Sedan 4D	2009	\$21,820	\$10,800	49.5%
Compact Car	Kia	Spectra	EX Sedan 4D	2009	\$15,850	\$8,100	51.1%
Compact Crossover	Hyundai	Tucson	GLS Sport Utility 4D	2009	\$20,695	\$10,600	51.2%
Compact Car	Chevrolet	Cobalt	LT Sedan 4D	2009	\$17,295	\$8,900	51.5%
Mid-Size Car	Chevrolet	Malibu	LT Sedan 4D	2009	\$22,990	\$11,775	51.2%
Mid-Size Car	Honda	Accord	LX Sedan 4D	2009	\$22,225	\$11,625	52.3%
Compact Crossover	Ford	Escape	XLT Sport Utility 4D	2009	\$26,185	\$13,750	52.5%

Source: Kelley Blue Book Automotive Insights

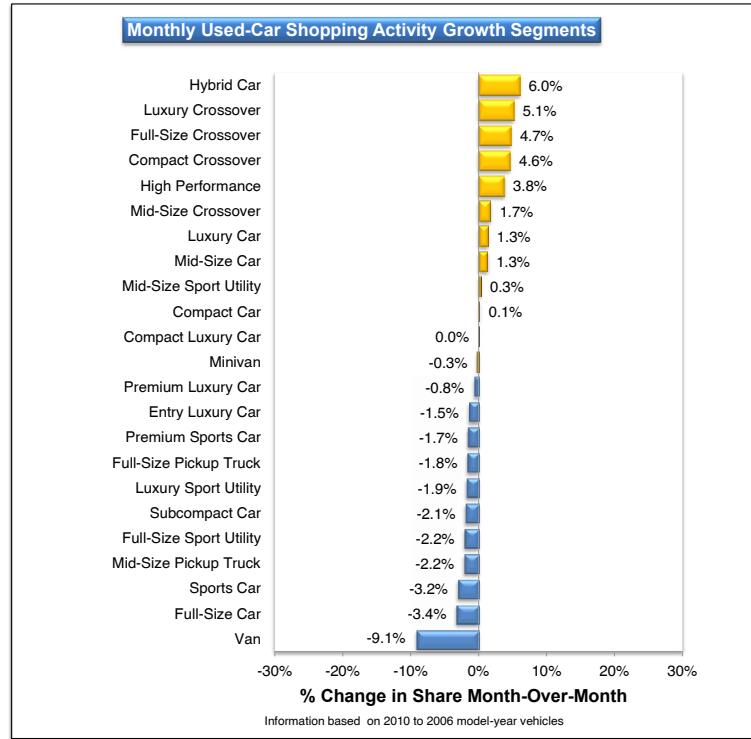
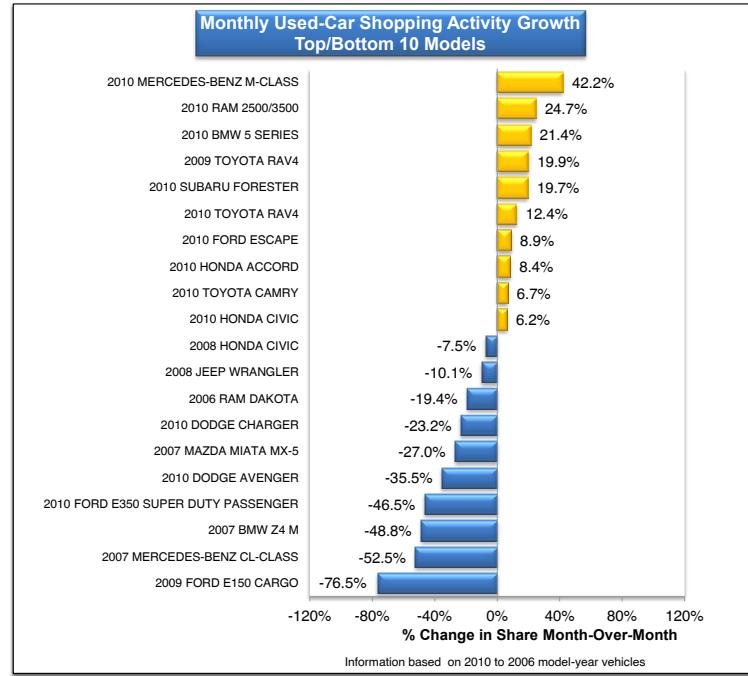
This commentary focuses on model years 2009-2011. The statements set forth in this publication are the opinions of the authors and are subject to change without notice. This publication has been prepared for informational purposes only. Kelley Blue Book assumes no responsibility for errors or omissions.

M-Class is Best-in-Class

- Arthur Henry, manager of market intelligence and market analyst, Kelley Blue Book

Kelley Blue Book's Hot Used-Car Report captures monthly used-car shopper activity on kbb.com, including a list of the top and bottom movers in the same time period. Results are provided by the Kelley Blue Book Market Intelligence Team, in an effort to help dealers better understand which used vehicles consumers are looking at most each month.

The 2010 Mercedes-Benz M-Class increased its traffic share more than any other used car during July: 42 percent month-over-month. For those dealers who currently have the M-Class on their lots, it is currently valued at \$13,500 less than the Fair Purchase Price of a brand new M-Class. Consumers who shopped the 2010 M-Class in July also researched vehicles in the entry-level luxury segment. The top models that were cross-shopped among entry-level vehicles were the Mercedes-Benz C-Class, BMW 3-Series and Audi A4, respectively. Other luxury SUVs that are highly cross-shopped include the BMW X5 and Lexus RX. In general, used M-Class shoppers are attracted to the luxury space and are looking to spend roughly \$28,000 to \$35,000 for their next vehicle.



About Kelley Blue Book (www.kbb.com)

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