PARTICIPANTS

Corporate Participants

Douglas W. Busk – Senior Vice President & Treasurer & Head-Investor Relations
Brett A. Roberts – Chief Executive Officer

Other Participants

Nick Zulovich – Editor, SubPrime Auto Finance News
John M. Hopkins – Analyst, Chartwell Investment Partners LP
Kevin F. O'Keefe – Analyst, Brown Advisory LLC

MANAGEMENT DISCUSSION SECTION

Operator: Good day everyone and welcome to the Credit Acceptance Corporation Fourth Quarter 2012 Earnings Call. Today's call is being recorded. A webcast and transcript of today's earnings call will be made available on Credit Acceptance's website.

At this time, I would like to turn the call over to Credit Acceptance Senior Vice President and Treasurer, Doug Busk.

Douglas W. Busk, Senior Vice President & Treasurer & Head-Investor Relations

Thank you, Sayed. Good afternoon and welcome to the Credit Acceptance Corporation Fourth Quarter 2012 Earnings Call. As you read our news release posted on the Investor Relations section of our website at creditacceptance.com, and as you listen to this conference call, please recognize that both contain forward-looking statements within the meaning of federal securities law.

These forward-looking statements are subject to a number of risks and uncertainties, many of which are beyond our control and which could cause actual results to differ materially from such statements. These risks and uncertainties include those spelled out in the Cautionary Statement Regarding Forward-Looking Information included in the news release. Consider all forward-looking statements in light of those and other risks and uncertainties.

Additionally, I should mention that to comply with the SEC's Regulation G, please refer to the Adjusted Financial Results section of our news release, which provides tables showing how non-GAAP measures reconcile to GAAP measures.

Consistent with last quarter, we will no longer be doing an overview of the quarter as part of the earnings call and will use this call to answer your questions. At this time, Brett Roberts, our Chief Executive Officer, Ken Booth, our Chief Financial Officer and I will take your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. Ladies and gentleman on the phone line, if you have a question at this time, please press star then one on your touchtone telephone. If your questions have been answered and you wish to remove yourself from the queue, please press the pound key. Once again ladies and gentleman if you have a question at this time, please press star then one on your touchtone telephone. One moment for our participants to queue up. We have a question from Nick Zulovich from SubPrime Auto Finance.

<Q – Nick Zulovich – SubPrime Auto Finance News>: Good afternoon, gentlemen. Thank you for the time today.

<A – Doug Busk – Credit Acceptance Corp.>: Sure.

<Q – Nick Zulovich – SubPrime Auto Finance News>: To start off, just wanted to get your overall assessment on the full year financial performance of the company. What metrics stood out to you as performing well in the calendar year?

<A – Doug Busk – Credit Acceptance Corp.>: Well, we are certainly pleased with the credit quality and the profitability of the business that we've originated, not only in 2012, but in 2011 and prior years. Our financial performance continued to be very strong. On the other side of the ledger, origination volume was lower than it had been in prior years and we believe this reflects the more intense competitive environment that we operated in during 2012.

<Q – Nick Zulovich – SubPrime Auto Finance News>: I also noticed from the release this afternoon that both the levels of active dealers, as well as new dealers, increased in the fourth quarter. What factors do you attribute those positive gains to?

<A – Doug Busk – Credit Acceptance Corp.>: We operate in a very large and fragmented market. There are over 50,000 dealers in the United States. As you see can see from our press release, we do business with a fraction of those. So there has been an opportunity that we've taken advantage of over the last several years to increase our active dealer base by enrolling new dealers on the program.

<Q – Nick Zulovich – SubPrime Auto Finance News>: Okay. And finally, you touched on it briefly, but what's your assessment of the competitive landscape that you operate in now, be it other companies dipping into the subprime market or established lenders potentially reaching down further into the credit spectrum? What's your assessment of the landscape that we operate in nowadays and how is Credit Acceptance prepared to handle it?

<A – Doug Busk – Credit Acceptance Corp.>: Well, as I mentioned before, the environment that we're in today is very competitive. There are hundreds of companies that serve the sub-prime auto space across the country. We have historically found that the primary factor that impacts how competitive the environment is, is the availability of capital to the industry. At the current time, capital is readily available and due to the low interest rate environment, capital is very cheap. That has led to an increase in competition.

We're responding in much the same way that we did in 2006 and 2007, which was the last competitive period in our industry. We are letting our loans per active dealer decline as the competition heats up and continue to grow our business by adding new dealers to the program.

<Q – Nick Zulovich – SubPrime Auto Finance News>: Very good. Thank you, gentlemen.

Operator: Thank you. Again ladies and gentleman if you have a question at this time, please press star then one on your touchtone telephone. And our next question comes from John Hopkins from Chartwell Investment.

<Q – John Hopkins – Chartwell Investment Partners LP>: Good afternoon. I see that in your expense write-up, you had an incremental fee for a third-party vendor termination. What was that related to?

<A – Brett Roberts – Credit Acceptance Corp.>: We have a relationship with a third party that provides the GPS-SID devices that are included in about half the loans that we write, that are installed on the vehicles. We switched providers, and the expense will cover servicing those devices in the future.

<Q – John Hopkins – Chartwell Investment Partners LP>: Okay. When we talk about that competitive pressure that you're obviously under, I mean, your spreads have come in quite a bit in the last few years...

<A – Brett Roberts – Credit Acceptance Corp.>: Can you speak up just a little bit? We're having trouble hearing you.

<Q – John Hopkins – Chartwell Investment Partners LP>: Sure, absolutely. In regards to that competitive pressure, are there other services or other ways that you can actually try to recapture some of the spreads that you've obviously lost in the last couple years?

<A – Brett Roberts – Credit Acceptance Corp.>: Not at this time. We're focused on our core product, which is what we're good at. We've been working on this product for a long, long time. We know what we're good at. We're just going to continue to offer our product. As Doug mentioned, we have a very small market share. So there's plenty of dealers that could benefit from our product that don't have it today. And so we're going to focus on expanding our business that way.

<Q – John Hopkins – Chartwell Investment Partners LP>: What's the principal way that you reach out to those dealers? I see that your origination expenses haven't increased significantly in the last year?

<A – Brett Roberts – Credit Acceptance Corp.>: We have a field sales force.

<Q – John Hopkins – Chartwell Investment Partners LP>: Okay. So it's out through the sales force?

<A – Brett Roberts – Credit Acceptance Corp.>: Yeah and actually those expenses have increased considerably for the sales force year-over-year -

<Q – John Hopkins – Chartwell Investment Partners LP>: Yeah. I did see that, yeah, absolutely.

<Q – John Hopkins – Chartwell Investment Partners LP>: But just internally, I see you haven't added much in the way of originations. Let me ask you if I'm looking at this right. It seems to me that you deployed about $350 million of additional average capital during the quarter, and your economic profit only rose $3.3 million in the same time period. So is that – that's kind of less than a 1% return on that average capital.

<A – Brett Roberts – Credit Acceptance Corp.>: No. I think the way to look at it is average capital, quarter over quarter. So, fourth quarter over the same period last year increased by about 23%.

<Q – John Hopkins – Chartwell Investment Partners LP>: Yeah, $353 million.

<A – Brett Roberts – Credit Acceptance Corp.>: Pardon me?

<Q – John Hopkins – Chartwell Investment Partners LP>: $353 million.

<A – Doug Busk – Credit Acceptance Corp.>: That's correct.

<A – Brett Roberts – Credit Acceptance Corp.>: In percentile terms, let me just frame the answer that way 23%, earnings per share, up 17.5%. The difference between the two is lower returns, but if you look at it over a long period of time, our returns are still at the high end of the historical range. Obviously, our return on equity and returns on capital are very, very healthy at this point.

<Q – John Hopkins – Chartwell Investment Partners LP>: Yeah. They're down 400 basis points, if I look at your adjusted return on capital of 14.5% in the most recent quarter, that's obviously down from what I see as a peak. I don't have all of the run here, but March 31, 2011 the quarter was 18%.

<A – Brett Roberts – Credit Acceptance Corp.>: Right.

<A – Doug Busk – Credit Acceptance Corp.>: Yeah.

<Q – John Hopkins – Chartwell Investment Partners LP>: So, I'm still looking at the fact is that you've deployed $350 million worth of capital, but you've only earned economic profit of $3.3 million on that. That looks like a pretty low return for the incremental capital versus prior periods.

<A – Brett Roberts – Credit Acceptance Corp.>: Yeah, I don't think that's the way to look at it.

<Q – John Hopkins – Chartwell Investment Partners LP>: Well, I know, but it's dollars, right? I mean that's the way to look at it, it's cash.

<A – Brett Roberts – Credit Acceptance Corp.>: We earned 14.5% on $1.9 billion roughly in capital, which is – and if you look at our returns over a long period of time, although they did spike as we went through the financial crisis, which is an unusual period, our returns today are at the high end of the historical range, primarily due to lower expenses as we've grown the business. But no question it's more competitive out there than it was just following the financial crisis, which means the returns we earned in those years probably aren't sustainable.

<Q – John Hopkins – Chartwell Investment Partners LP>: No, right. And obviously part of the 14.5% return on capital incorporates prior periods that are still returning and earn a rate of return on capital that was better previously than it is now?

<A – Brett Roberts – Credit Acceptance Corp.>: Correct.

<A – Doug Busk – Credit Acceptance Corp.>: Yep.

<Q – John Hopkins – Chartwell Investment Partners LP>: Right. Tell me, and forgive me for not remembering this. Are there regions of the country where you are particularly stronger than others?

<A – Brett Roberts – Credit Acceptance Corp.>: Yes.

<A – Doug Busk – Credit Acceptance Corp.>: Yeah, I mean, we certainly we have a very strong presence in Michigan. Other strong states for us would be New York, Ohio, Texas. We're strong in the Southeast, Alabama and Mississippi.

<Q – John Hopkins – Chartwell Investment Partners LP>: And are you seeing a concerted effort by one or two of your competitors in your markets, or are a bunch of little guys just chipping at you everywhere?

<A – Brett Roberts – Credit Acceptance Corp.>: It's a huge market. I mean, as Doug mentioned, there are hundreds of companies that play in this space. So it's not important what any single or handful of competitors do. It's really the entire market, it is getting more competitive.

<Q – John Hopkins – Chartwell Investment Partners LP>: Okay. So you're not really seeing a concerted effort by one or two of your largest competitors?

<A – Brett Roberts – Credit Acceptance Corp.>: No, I mean there is certainly market share statistics out there. You see who was growing the fastest, but even the largest participant in our space still has a very small market share.

<Q – John Hopkins – Chartwell Investment Partners LP>: Right, right. Okay, great. Thanks, gentlemen.

<A – Brett Roberts – Credit Acceptance Corp.>: Yeah.

Operator: Thank you. Again ladies and gentleman if you have a question at this time, please press star then one on your touchtone telephone. Our next question comes from Kevin O'Keefe from Brown Advisory.

<Q – Kevin O'Keefe – Brown Advisory LLC>: Hey, guys. Thanks for taking my question. Couple questions for you. First, I was hoping you could just frame the market a little further for me. So you mentioned there's 50,000 dealers, and if I'm reading your release correctly, you penetrated only 4,000 of those, is that right?

<A – Doug Busk – Credit Acceptance Corp.>: Correct.

<Q – Kevin O'Keefe – Brown Advisory LLC>: Okay. And then – are you the largest player in the market?

<A – Brett Roberts – Credit Acceptance Corp.>: It depends on how you define the market, but we're certainly in the top five depending on what Beacon score cutoff you use.

<Q – Kevin O'Keefe – Brown Advisory LLC>: Okay. So say like, on a dollar loan basis, I'm trying to understand like how big the subprime auto market is now and what your share is?

<A – Brett Roberts – Credit Acceptance Corp.>: Again, it depends. Give me a Beacon score cutoff, and we could answer that question. It's somewhere in the 2% to 5% range, depending on what sort of definition of the market you use.

<A – Doug Busk – Credit Acceptance Corp.>: There are about 40 million used vehicles sold annually, there are about 70 million adults with credit scores of 640 and below. About half of those have credit scores with 550 and below. So, again, you can chop the market up a lot of ways, but it's a pretty big market, and we have a small share of it, any way you look at it.

<Q – Kevin O'Keefe – Brown Advisory LLC>: Okay. And so as you think about – you mentioned that you have a field sales force. How is your expansion strategy, like, what specifically are you guys doing to grow the share to where you've increased your active dealers by 25%? It seems like you're trying to spread out to mitigate some of the market risk, and I'm just curious, is that just – do you just open up shop in a submarket and start hiring people, or how does that work?

<A – Brett Roberts – Credit Acceptance Corp.>: We've covered the entire country for quite a while, so every ZIP code in the country was assigned to a salesperson. So all we did was shrink the size of the territories in order to more effectively cover the geography. So that we went from roughly 150 salespeople to 250, and we did that just by changing the size of the territories. And what we find is, the larger the territory there's just areas where the salesperson wasn't effectively covering his entire territory. So with smaller territories, we're able to reach more dealerships.

<Q – Kevin O'Keefe – Brown Advisory LLC>: Do you have a plan for 2013 as far as sales force expansion?

<A – Brett Roberts – Credit Acceptance Corp.>: We do. In 2013, we will probably sort of consolidate where we are today in terms of the total number. We went through a very rapid expansion, and so naturally we're going to have some attrition and we're going to have to rehire in certain areas for people that don't work out. So we are probably going to be right around where we are today, may be a little bit more.

<Q – Kevin O'Keefe – Brown Advisory LLC>: And then as you think about that, is there a lag effect from your hires where you still see that your production should mirror, to some extent, the growth that you've been able to put up these last few years, should be able to mirror recent years? Are some of these employees just now ramping up?

<A – Brett Roberts – Credit Acceptance Corp.>: No question about it. It takes a while for a salesperson to hit the ground and then become productive. Over a long period of time, so if you pick up five or 10 year periods of growth, unit volumes have been roughly the same as the growth in the size of the sales force. Obviously that's not holding true this year because of the competitive environment but certainly the plan is for those numbers to come in line over a long period of time.

<Q – Kevin O'Keefe – Brown Advisory LLC>: Okay. And then just one more question if I could. Just thinking about the spread that you guys are putting up, you mentioned it's starting to get towards that 2006, 2007 type competitive environment. I'm just curious, given how much lower prevailing rates are now, should we think about that the baseline spread would actually be lower than where we were in 2006-2007? So, i.e., like there's still a lot more spread to give up given where the rest of the market is relative to where we were in 2006-2007?

<A – Brett Roberts – Credit Acceptance Corp.>: That's one way to think about it. I would say it a little bit differently. The cost of capital is low, the capital is available. So we're going to see more competition. I mean, we're going to price it to achieve the maximum amount of economic profit. So we balance unit volume and profit per loan in order to optimize that equation, and the point where it's optimized is going to be a more aggressive price, or more money out the door than what it would have been in 2007 to achieve the same result, just because the cost of capital is lower.

<Q – Kevin O'Keefe – Brown Advisory LLC>: Got you, okay. Cool. Thanks, guys.

Operator: Thank you. We have a follow-up question from John Hopkins from Chartwell Investment.

<Q – John Hopkins – Chartwell Investment Partners LP>: Follow-up actually on that point just a bit. Is there a spread level – given that your expense base is significantly higher than it was in 2006-2007, is there a spread level where you're going to have to be forced to walk away from business? And I mean materially reduce your activity?

<A – Brett Roberts – Credit Acceptance Corp.>: Our expenses, the way we look at that would be as a percentage of capital. So obviously we've improved our position relative to the 2006-2007 periods that you referenced. But there clearly is a point where business is unprofitable, and we certainly don't plan to write any unprofitable business.

<Q – John Hopkins – Chartwell Investment Partners LP>: If we look at the forecasted collections and I see now in 2009, you were almost at an 80% forecasted collection, and it's come down materially since then, is that also a result of the competitive pressure? Are you forced to write business that's less I'll say robust than it was three years ago?

<A – Brett Roberts – Credit Acceptance Corp.>: I think the thing to focus on there is the performance relative to our initial expectation. So we don't really care what the absolute collection rate is as long as it's what we thought it was going to be when we wrote the loan.

<Q – John Hopkins – Chartwell Investment Partners LP>: Right.

<A – Doug Busk – Credit Acceptance Corp.>: Because, yeah, we're varying the amount of the advance to the dealer based on the expected performance of the loan. So the key isn't just the absolute collection rate, it's whether our forecast at origination proves to be accurate.

<A – Brett Roberts – Credit Acceptance Corp.>: So obviously what happened in 2009 is we saw a very large positive variance relative to what we thought when we wrote the loans.

<Q – John Hopkins – Chartwell Investment Partners LP>: Yes.

<A – Brett Roberts – Credit Acceptance Corp.>: We were perhaps in retrospect too conservative, and we also know that business that's originated with little competition tends to perform better than business that's originated when there's lots of competition.

<Q – John Hopkins – Chartwell Investment Partners LP>: Right.

<A – Brett Roberts – Credit Acceptance Corp.>: And so we had that working for us on the 2009 originations.

<Q – John Hopkins – Chartwell Investment Partners LP>: Are you seeing any material tick up in the, in your charge-offs? I didn't really notice a significant, but you probably have a better look through than I do.

<A – Brett Roberts – Credit Acceptance Corp.>: Because we booked the loan initially at the expected performance, charge-offs really aren't an important metric for us. Really the important metric would be the one that's on page 2 of the release that just shows the actual performance relative to our expectations.

<Q – John Hopkins – Chartwell Investment Partners LP>: Right, right. So, let me ask you another question real quick, just so I can understand these numbers well. The spread obviously excludes any holdback or accelerated holdback. So the fact that the holdback numbers or the accelerated holdback numbers may actually be higher, the spread that's shown here may actually be lower. Is that correct?

<A – Brett Roberts – Credit Acceptance Corp.>: I mean holdback is money that goes out the door after the advance has been repaid.

<Q – John Hopkins – Chartwell Investment Partners LP>: Right.

<A – Brett Roberts – Credit Acceptance Corp.>: So I wouldn't deduct holdback from the spread necessarily. The spreads are just an indicator, a rough indicator of how we price the loans to give investors an idea of which way the market is going, which way our pricing is going.

<Q – John Hopkins – Chartwell Investment Partners LP>: Right. So if I theoretically created a net spread column, I would actually deduct the percentage of those holdback and dealer holdbacks that go back to the dealer after the fact, right?

<A – Brett Roberts – Credit Acceptance Corp.>: It's not something – I mean we've been doing this a long time, and it's not something we've ever looked at.

<Q – John Hopkins – Chartwell Investment Partners LP>: Okay.

<A – Brett Roberts – Credit Acceptance Corp.>: I mean we can certainly look at it that way, but it's not something the company has found useful.

<Q – John Hopkins – Chartwell Investment Partners LP>: Right, okay. Great., Thanks, gentlemen.

<A – Brett Roberts – Credit Acceptance Corp.>: Yeah.

Operator: Thank you. Our next question comes from Kevin O'Keefe from Brown Advisory.

<Q – Kevin O'Keefe – Brown Advisory LLC>: Hey, guys, just one more follow-up. You gave some great stats on the used vehicle market and I'd just be curious if you had any comment on the whole rolling junkyard theme and if you feel like your borrowers have extended the life of their autos to any sort of level that it makes you think that either there is a huge build up in demand. Ultimately when we see a more broad based economic recovery or if your type of borrower is more kind of a just in time shorter auto life kind of borrower to where this whole rolling junkyard, 11 year average life of cars, I think, doesn't really play into your borrowing base?

<A – Brett Roberts – Credit Acceptance Corp.>: I don't think that's going to be an important thing to watch in terms of our results. Typically, our results are determined more by the competitive environment, cost of capital, those types of overall sort of macro indicators, things like the price of used cars, some of these theories, like you mentioned, they haven't been important to us over time.

<Q – Kevin O'Keefe – Brown Advisory LLC>: Okay, cool. And just last one, if you could comment just on your thoughts about capital management? You're pretty aggressive in buying back stock last year. Just any incremental thoughts on how you're thinking about that heading into the New Year?

<A – Doug Busk – Credit Acceptance Corp.>: Well, we continue to think about it the same way. Our primary objective from a capital management perspective is to make sure that we have the capital that we need to fund anticipated origination levels. So, if the answer to that question is yes and we have the opportunity to buy stock back at less than what we believe the intrinsic value is, than we will return cash to shareholders. So, no change there from the historical way in which we've managed it.

<Q – Kevin O'Keefe – Brown Advisory LLC>: Okay, cool. Thanks, guys.

Operator: Thank you. We have another follow-up from John Hopkins from Chartwell Investment.

<Q – John Hopkins – Chartwell Investment Partners LP>: Given kind of where we are in cost of capital cycle, I was kind of wondering what steps you may be considering to kind of potentially lock-in a current cost of capital as if in fact we're kind of about to move up the cycle and that cost of capital is about to change for the negative for you?

<A – Doug Busk – Credit Acceptance Corp.>: We already have in excess of 50% of our debt that is fixed rate in nature. So, we're already reasonably protected from that perspective. We also employ less financial leverage than most others in the industry. So, our exposure to a rising rate environment is less than most others in the industry. So we feel pretty good about the liability side of our balance sheet at the current time.

<Q – John Hopkins – Chartwell Investment Partners LP>: Thank you.

Operator: Thank you. With no further questions in queue, I would like to turn the conference back over to Mr. Busk for any additional or closing remarks.

Douglas W. Busk, Senior Vice President & Treasurer & Head-Investor Relations

We would like to thank everyone for their support for joining us on our conference call today. If you have any additional follow-up questions, please direct them to our Investor Relations mailbox at ir@creditacceptance.com. We look forward to talking to you again next quarter. Thank you.

Operator: Once again, this does conclude today's conference. We thank you for your participation.