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Op-Ed

Why I'm shorting a taxi medallion lender

By James F. Hickman
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New York's yellow taxis are not at risk of extinction, but the economic model historically supporting taxicab medallions is on life support, and the implications are serious for medallion owners and lenders with significant asset exposure like Medallion Financial, Signature Bank and numerous credit unions.

The yellow-cab industry in the city is roughly $2.5 billion per year. All of those dollars were historically captured by 13,605 taxi medallions—only about 200 more than existed in the 1930s. The supply cap and monopolistic structure drove medallion prices above $1 million in 2013.

But getting larger in the yellow cab's rear-view mirror were Uber and other free-market-based, for-hire vehicles that are summoned by app—not by hand as yellow cabs are—and are generally lower-priced, higher-quality and offer better customer service. Uber only hit its stride in New York in July 2014, after dropping its non-peak prices to below taxi fares and launching a recruitment drive that by December had increased its driver count to 16,000 from 7,000.

This rapidly growing supply has not only diluted taxi revenue, it has drawn drivers who would otherwise be leasing medallions. Except when undergoing maintenance, yellow cabs used to be on the streets nearly all the time, but sources and public statements indicate that idle time is up substantially—as much as 20% at some garages. That means fewer dollars flowing to taxi-medallion-owners. The result? Medallion foreclosures for the first time in years, including Citibank's recent move to seize 90 medallions owned by New York taxi mogul Gene Freidman.

If medallions were no longer required to pick up riders, why would anyone buy a superfluous piece of metal? They did not in Minneapolis, Milwaukee and San Diego after supply caps were eliminated and legal efforts by medallion owners failed. Medallions became valueless relics once they ceased to confer exclusive access to vehicle-for-hire markets.

The end game in New York City is not an elimination of taxis from the road, but stable co-existence in a freer market, with significantly lower medallion values. That's a problem for medallion owners and lenders who bought and lent at prices that require greater cash flow than yellow cabs now generate. And those revenues are still falling.

Medallion-bearing taxis are burdened by significant costs not shared by Uber and other ridesharing drivers, namely lease fees and debt service. Eventually, as gross meter revenue continues to be diluted, medallion costs will have to be eliminated for taxi drivers to remain competitive.

Just as people walked away from their homes when the recession hit, medallion owners short on cash when a mortgage balloon payment is due and who lack equity in their medallions will have no choice but to default. Taxi medallions will be seized and resold at lower prices.

For companies like Medallion Financial and Signature Bank, low historical default rates when structural taxi supply shortages existed are not predictive of a future that includes unconstrained, free-market-based new supply. Medallion Financial showed an increase in its medallion loan-to-value ratio to 60% from 40% between September and December and an increase in its late payments to the highest levels since 2010. The trends do not lie.

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