

BUSINESS

Auto-Parts Companies' Bankruptcies Rattle Credit Markets—What to Know

Failures among auto-parts firms and subprime lenders may signal broader risks, but a strong economy and falling rates limit spillover, analysts say.



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A road sign at the foothills of the Great Smoky Mountains in Kodak, Tenn. Darlene McCormick Sanchez/The Epoch Times



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10/17/2025 | Updated: 10/17/2025

The U.S. economy has remained resilient in recent months, but auto-parts companies have not. The increasing number of bankruptcies in the auto parts industry is unsettling the high-yield credit markets.

This upheaval is making it increasingly difficult for low-income consumers to purchase cars, and is also compelling banks and financial institutions to write off loans to these failed companies.

On June 11, auto parts supplier Marelli Holdings Co. Ltd. [filed](#) for Chapter 11 cases in the United States Bankruptcy Court for the District of Delaware to restructure its long-term debt obligations.

On Aug. 18, Car Toys, which [describes](#) itself as “the largest independent multi-channel specialty car audio and mobile electronics retailer in America, with multiple locations across the western U.S.,” [filed](#) for bankruptcy.

On Sept. 10, Tricolor and nearly a dozen of its affiliates each [filed](#) a petition in the United States Bankruptcy Court for the Northern District of Texas to transition from Chapter 11 of the United States Code to Chapter 7.

This transition allows Tricolor to move from reorganization to liquidation, which involves the ending of the business and the selling of assets.

Founded in 2007, Dallas-based Tricolor is a chain of used-car dealerships and a primary subprime auto lender. It operates in several states and serves thousands of low-income individuals, including those with low credit or no credit.

Tricolor’s business model was unique in its use of individual taxpayer identification numbers (ITINs) instead of Social Security numbers. This approach enabled individuals with limited or no documented U.S. credit history to access credit. The strategy was instrumental in serving thousands of low-income individuals, including those in immigrant communities.

“Remember, too, that many of these loans were made at a time when credit scores were higher than they would normally be due to pandemic-era programs like paused student loans,” Chris Motola, a financial analyst at NationalBusinessCapital, told The Epoch Times.

“At the same time, car prices skyrocketed. So you had easy credit, people taking out larger loans, inflation, and, more recently, weakness in the job market.”

On Sept. 28, First Brands Group LLC and 98 affiliated debtors [filed](#) for Chapter 11 bankruptcy with the United States Bankruptcy Court for the Southern District of Texas.

The failure of these auto parts companies has sent shockwaves through the high-yield or junk credit markets, with the ICE BofA U.S. High Yield Index [rising](#) by nearly 50 basis points since mid-September.

The index, also known as the High-Yield OAS, measures the average premium (extra yield or spread) corporate debt investors demand to hold U.S. high-yield corporate bonds instead of U.S. Treasury bonds.

The spike in high bond yields raises the cost of financing for borrowers with low credit scores, often low-income Americans, as they struggle to cope with the still-elevated cost of living and a weakening labor market.

Meanwhile, lenders of these failed companies are facing hefty losses, as they must write off these loans.

This week, JPMorgan Chase [disclosed](#) a \$170 million charge-off related to the bank’s wholesale lending to subprime lender Tricolor, a dark spot in an otherwise robust earnings report.

A charge-off is a term banks use to describe unpaid debt that has been written off as a loss.

Meanwhile, Jefferies Financial [expects](#) to incur a \$43 million loss resulting from First Brands’ failure.

The situation worsened toward the end of the week, as a couple more regional banks—Western Alliance Bancorp and Zions Bancorp—announced write-offs, prompting a sell-off on Wall Street.

“Auto-related bankruptcies of companies like First Brands and Tricolor signal stress in pockets of corporate lending to consumer-facing companies, but they also reflect consumer demand headwinds likely to impact other

industries,” Joseph Raetzer, a corporate, M&A, and Securities attorney, told The Epoch Times.

He said that sustained low consumer sentiment, higher interest rates, and longer replacement cycles point to broader pressure that could extend to other industries such as consumer electronics, major appliances, and furniture.

Raetzer believes that corporate lenders must reorient underwriting discipline across the board, considering these new trends.

“These auto-related bankruptcies are the smoke signaling a coming fire in consumer-facing company earnings, which will result in more losses to corporate lenders,” he said.

Doug Burnetti, founding attorney of Burnetti, P.A., and an auto law specialist, believes the recent failures of auto-parts suppliers and subprime auto lenders are warning signs for the broader transportation sector.

“These bankruptcies show how shaky underwriting and off-balance-sheet debt can cascade quickly through parts supply chains and ultimately impact the cost and reliability of vehicles,” he told The Epoch Times.

However, these failures occur at a time when the U.S. economy remains resilient and interest rates are decreasing, reducing the likelihood that business failures in the auto parts industry will spread to other companies and sectors.

Gimme Credit senior bond analyst Jay Cushing believes it’s too soon to tell whether the bankruptcies of Tricolor and First Brands are “canaries in a coal mine” or just idiosyncratic pockets of weakness in deep subprime or one-off cases of potential fraud.

“In either case, these events are likely to lead to incrementally tighter lending standards that could have a cooling effect on credit availability and ultimately car sales, a trend that the audience should be cautious about,” he told The Epoch Times.



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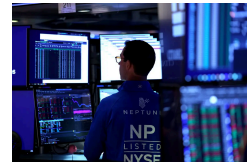
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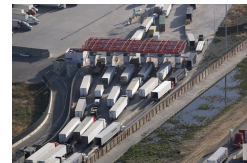
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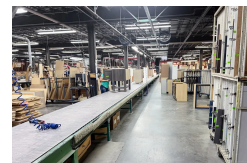
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