

# RECESSION, SCRAPPAGE AND SUSTAINABLE RECOVERY

*A report by Peter N C Cooke*

*in association with BCA*



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Professor of Automotive Management  
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# Executive Summary

This independent report seeks to review the impact of the recession on new car sales in the United Kingdom, the new car scrappage scheme and the impact of these factors on sustainable recovery of the UK car market.

The key issues raised in the report might be summarised as follows;

- The new car market in the United Kingdom settled around the 2.5 million unit mark between 2001 and 2005; a figure that is now widely considered unsustainable in the longer term. Despite support from the scrappage programme, UK new car volumes dipped below two million units in 2009.
- The UK scrappage scheme is one of several introduced across Europe; the largest and arguably most successful in Germany. Close to 400,000 new cars and LCVs had been ordered under the UK scrappage scheme when it closed on 31st March 2010. Scrappage deals accounted for around a fifth new car registrations between May 2009 and March 2010 – the balance of some 20,000 orders to be delivered by the end of July. The bulk of the replacement units are small new cars at the lower end of the price scale, the vast majority imported.
- It is likely that somewhere between 10% and 15% of new cars supplied through the scrappage scheme will have been built in the UK – offering what can only be regarded as moderate support for the country's car manufacturing and its supply chain.
- There is considerable concern at what might take place when the scrappage scheme finishes; a hike in VAT, escalating fuel prices, rising VED and first year 'showroom taxes' could well signal a difficult period for the car market. The SMMT's latest forecast for the new car market is that it will fall to 1.817 million units in 2010 – down from 1.994 million in 2009 which was the first sub two million market since 1995.
- The report also looks at the aftermath of recession and the severe and prolonged downturn in new car volumes. It highlights there will be as many as three million fewer younger cars in the UK car parc over the next few years than the high point reached in 2005 and the need for dealers to counteract such a serious threat to their used car and aftersales business.
- Finally, the report makes some high-level recommendations for car manufacturers' and dealers' strategic planning, in the face of much changed market conditions.

The report is commended to senior executives of car manufacturers, the finance and leasing industry and those working in the automotive retail sector in particular.

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# Introduction

The economic downturn and recession of 2008 to 2010, driven by the banking and financial services crisis, has hit practically every global industry. Automotive industries are no exception. Globally, automotive manufacturing, with 25% or more installed excess capacity has long been overdue for restructuring – which has been radical and brutal to date and is not yet finished.

*Comments have focused almost entirely on the 'big ticket' end of the industry*

To date, public comments have focused almost entirely on vehicle manufacturers' circumstances – the 'big ticket' end of the industry. While the impact of recession has also been felt acutely in the retail motor sector and support industries, which employ more than three times as many people as manufacturing, this has typically gone pretty much unnoticed.

The current report has been prepared independently by the automotive team at the Centre for Automotive Management at The University of Buckingham Business School, led by Professor Peter N C Cooke.

## Report objectives

The range of issues that might be considered is enormous and beyond the scope of this short report, so the objectives have been tightly drawn. The data used has been confined to published material, while the analyses and their implications are purely those of the Automotive Group at the University.

The objectives of the review might be summarised as follows;

- To consider the impact of the current economic recession on European and UK automotive industries, exemplified by production and new car sales.
- To review car scrappage programmes introduced across Europe.
- To evaluate the objectives and outcome of the United Kingdom's scrappage scheme.
- Consider the development of the United Kingdom car parc, given a significant and prolonged reduction in new car sales.
- Propose a series of actions to support dealers in a period of sustainable recovery – with particular emphasis on the fast-changing shape of the UK automotive market.

Although the data will undoubtedly change over time, it is felt the overall thrust of the report will hold firm for the foreseeable future.

## Report format

The report is divided into the following chapters;

- **Chapter 2;** reviews recent sales and manufacturing outputs in western European countries, where current sales figures show most major new car markets have started to recover. The chapter summarises the EU scrappage programmes at a high level, together with a short review of the German experience.
- **Chapter 3;** focuses on the UK car market and the serious fall in new car volumes in the latter part of 2008 and early 2009 – and hopes for a sustained recovery. It also highlights some UK-specific issues associated with an industry structure where close to 80% of cars built in the UK are exported, and around 85% of new cars sold in the UK are imported.
- **Chapter 4;** presents an objective view of the United Kingdom’s scrappage scheme for cars and vans. Taxpayer support for the programme was increased from an initial £300million to £400 million at the end of September – and the scheme ultimately prolonged until the end of March 2010.
- **Chapter 5;** this chapter suggests a range of sustainable measures dealers might take to protect and develop their business and viability in the post-recession period.
- **Chapter 6;** pulls together relevant strands from the previous chapters and summarises the Centre for Automotive Management’s conclusions and strategic implications for car manufacturers, franchised dealers and the wider car industry.

*Serious fall in new car volumes in the latter part of 2008 and early 2009*

The Centre for Automotive Management Team has sought to take an objective, longer-term view of scrappage programmes and economic recovery which may differ in some respects from views expressed by other publications or interested parties.

# Recession and the European Automotive Industry

## European new car sales

With some notable exceptions, the 2008/2009 recession has driven down vehicle manufacture and sales volumes across Europe.

What is the natural demand and what is ‘forced feeding’ of new car markets in Europe is beyond the scope of this report. Figure 2[1] shows the new car registrations trend for western European countries between 1990 and 2009. It shows a fairly steady market trend for a decade leading up to 2007, before new car volumes fell back by over a million units for the succeeding two years.

With some exceptions, EU15/EFTA countries have mature automotive markets, although some are still developing.

Figure 2[1]; EU15/EFTA new car registrations;1990 – 2009

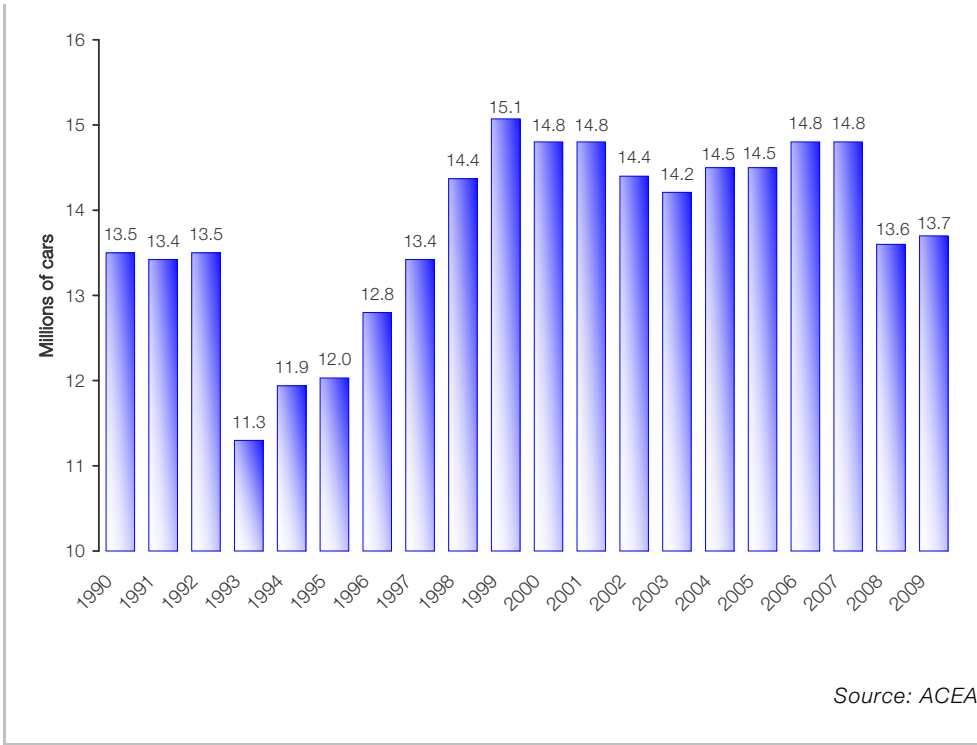
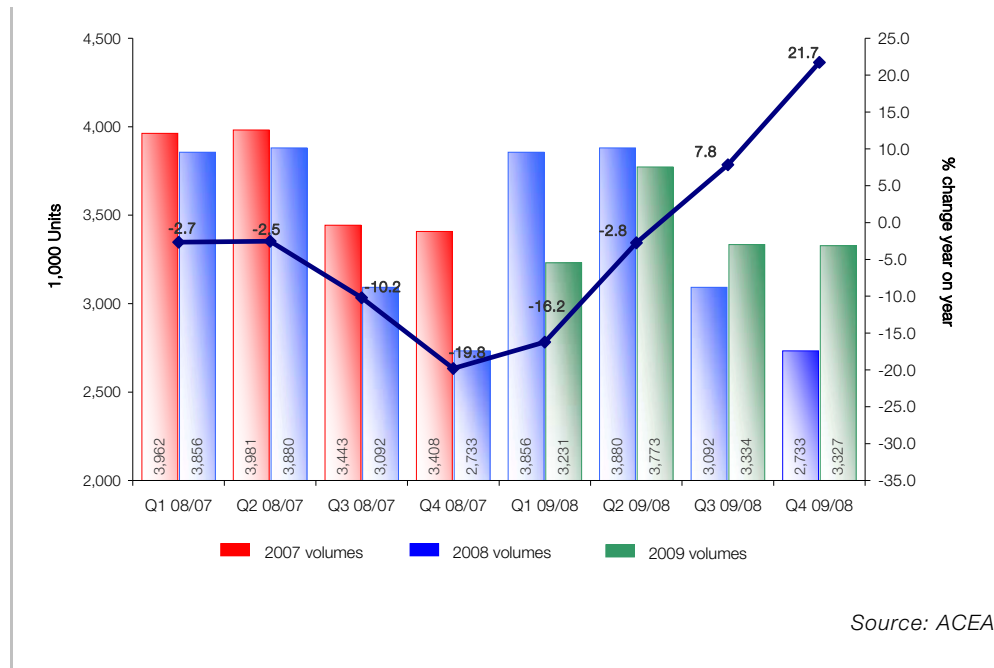


Figure 2[2] overleaf shows there was a serious drop in new car volumes between mid 2008 and mid 2009 in the EU15/EFTA market area.

*Surprising that full-year 2009 new car sales are higher than 2008*

The surprising result is that full-year 2009 new car sales for western Europe are some 100,000 units higher than 2008; scrappage schemes clearly playing a huge part in this, frankly, unlikely outcome. The challenge now is for 2010, with scrappage schemes finished or soon coming to an end.

Figure 2[2]; Quarterly EU15/EFTA new car registrations; 2007 – 2009



Source: ACEA

Figure 2[3]; EU15/EFTA new car registrations 2008 – 2009

	Jan - Dec 2008	Jan - Dec 2009	% Chg 09 vs. 08	Units 09 vs. 08
Austria	293,697	319,403	8.8	25,706
Belgium	535,947	476,194	-11.1	-59,753
Denmark	150,197	112,181	-25.3	-38,016
Finland	139,669	88,344	-36.7	-51,325
France	2,050,282	2,302,398	12.3	252,116
Germany	3,090,040	3,807,175	23.2	717,135
Greece	267,242	219,730	-17.8	-47,512
Ireland	151,607	57,457	-62.1	-94,150
Italy	2,161,682	2,158,901	-0.1	-2,781
Luxemburg	52,359	47,265	-9.7	-5,094
Netherlands	499,918	387,215	-22.5	-112,703
Portugal	213,389	161,013	-24.5	-52,376
Spain	1,161,176	952,772	-17.9	-208,404
Sweden	253,982	213,408	-16.0	-40,574
United Kingdom	2,131,795	1,994,999	-6.4	-136,796
<b>Europe (EU15)</b>	<b>13,152,982</b>	<b>13,298,455</b>	<b>1.1</b>	<b>145,473</b>
Iceland	9,033	2,113	-76.6	-6,920
Norway	110,617	98,675	-10.8	-11,942
Switzerland	288,557	266,049	-7.8	-22,508
<b>EFTA</b>	<b>408,207</b>	<b>366,837</b>	<b>-10.1</b>	<b>-41,370</b>
<b>EU15/EFTA</b>	<b>13,561,189</b>	<b>13,665,292</b>	<b>0.8</b>	<b>104,103</b>

Source; ACEA

Following a marked decline in the second half of 2008 and the first half of 2009, EU15/EFTA new car volumes picked up in the second half of last year, largely due to the impact of scrappage schemes in major markets. In total, 13,665,292 new cars were registered in 2009; 0.8% up on 2008 – but 7.4% and 1.13 million units fewer than 2007.

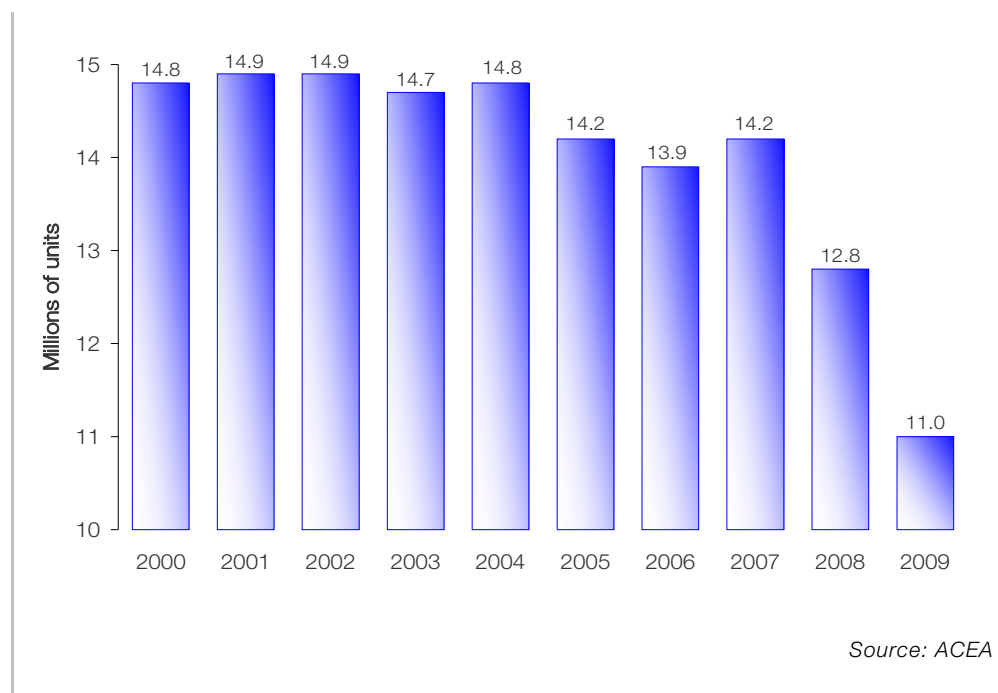
*In 2009, only Austria, France and Germany posted growth in new car volumes*

In 2009, only Austria (+8.8%), France (+12.3%) and Germany (+23.2%) posted growth in new car volumes compared to 2008 – although scrappage schemes also cushioned results in Italy (-0.1%), the UK (-6.4%) and Spain (-17.9%) – see Figure 2[3].

### EU15 new car production

EU15 car production, which accounts for around 80% of total European car output, held steady near the 15 million mark for several years up to 2004, falling thereafter to 12.8 million units in 2008 – Figure 2[4].

**Figure 2[4]; EU15 passenger car production 2000 – 2009**



Despite being bolstered by various scrappage initiatives, the downward trend in EU15 passenger car production intensified in 2009, down 14.1%, and 1.81million units year on year, to 11.03 million.

Figure 2[5] overleaf shows the hardest hit of the major car producers were the UK and France – the former’s car production down 30.9% to 999,460 for 2009, and the latter’s 15.1% lower at 1.82 million units. Germany’s car production held up better, however, down 10.3% to 4.96 million, as did Italy’s, rising 0.3% to 661,000 cars last year.

Figure 2[5]; EU15 car production; 2008 – 2009

Country	2008	2009	% Change 09/08	Units Change 09/08
Austria	125,836	56,000	-55.5	-69,836
Belgium	680,131	510,300	-25.0	-169,831
Finland	17,519	10,907	-37.7	-6,612
France	2,145,935	1,821,734	-15.1	-324,201
Germany	5,532,030	4,964,523	-10.3	-567,507
Italy	659,221	661,100	0.3	1,879
Netherlands	59,223	50,620	-14.5	-8,603
Portugal	132,242	101,680	-23.1	-30,562
Spain	1,943,049	1,812,688	-6.7	-130,361
Sweden	252,287	128,738	-49.0	-123,549
United Kingdom	1,446,619	999,460	-30.9	-447,159
<i>Double counting Germany/Belgium</i>	<i>132,402</i>	<i>80,300</i>	<i>-39.4</i>	<i>-52,102</i>
<i>Double counting Italy/EU</i>	<i>12,472</i>	<i>3,886</i>	<i>-68.8</i>	<i>-8,586</i>
<b>European Union EU15</b>	<b>12,849,218</b>	<b>11,033,564</b>	<b>-14.1</b>	<b>-1,815,654</b>

Source: ACEA

### Badly needed a kick start

With the multiplier effect on industry and employment through the supply chain, these disappointing sales and production figures suggest the European motor industry badly needed some form of ‘kick start’ to get it moving, with the implications of creating recovery elsewhere in the economy – a classic application of Keynesian economics.

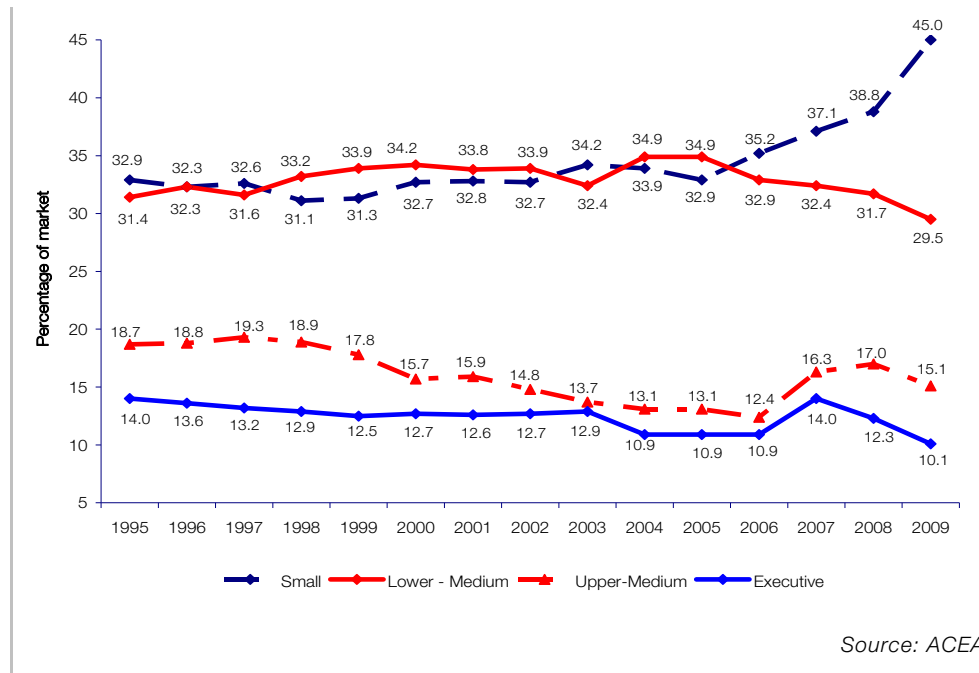
The ‘pump priming’ scrappage interventions were developed with the support of Brussels and began to emerge at the end of 2008. Broad rules were laid down for the type of support that could be offered, so national governments could develop programmes most suited to their domestic requirements – without financial support from the EU.

Realistically, it will be some considerable time before it is possible to make a wholly objective judgement on whether scrappage schemes were economically justified or were merely a short-term, very expensive, political expedient.

It will also be some time before it is possible to determine how much scrappage schemes have changed the profile of individual new car markets. As can be seen from Figure 2[6] overleaf, driven by scrappage incentives, the EU15 new car market has already swung sharply towards smaller cars, from 38.8% of the market in 2008 to 45% in 2009 – a growing proportion of which are being imported from the Far East.

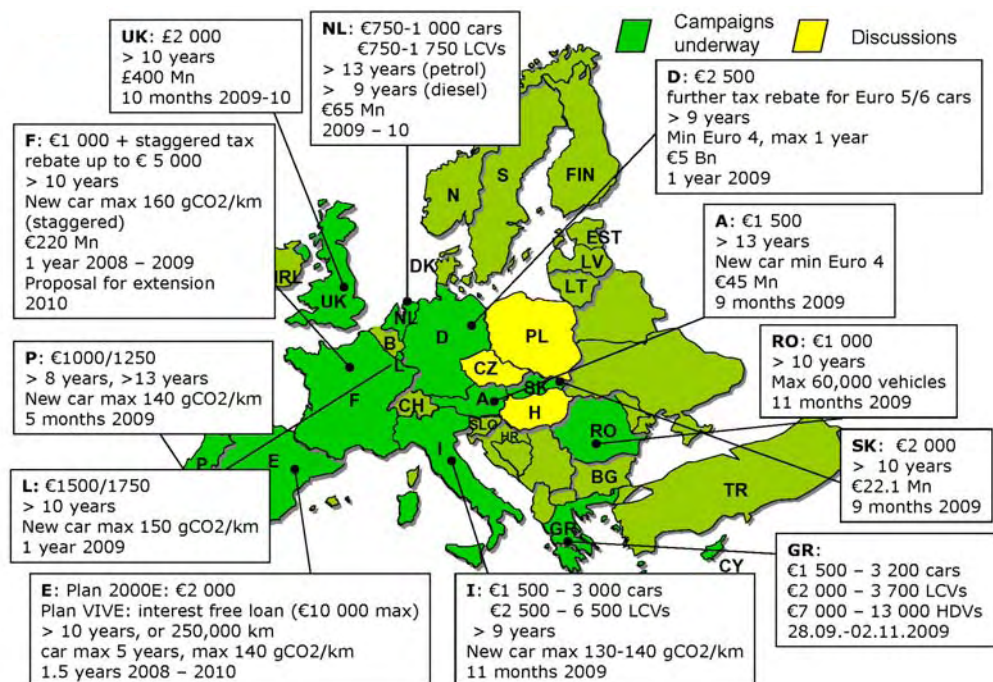
*The EU15 new car market has swung sharply towards smaller cars*

Figure 2[6]; EU15 car market share by segment 1995 -- 2009



While a shift to small cars of this magnitude may have substantial benefits in reducing the carbon footprint, it must have considerable implications as far as manufacturer and dealer profitability is concerned. As a rule of the thumb, there is surely much less profit to be made from selling a €10,000 car than a €20,000 one. Of course, as the effect of scrappage dies out in 2010, the ‘pendulum’ is likely to resume the gentler move to smaller cars experienced in recent years.

Figure 2[7]; Summary launch EU scrappage schemes



## EU scrappage schemes

While EU member states are part of a single economic community, the various countries' scrappage programmes outlined in Figure 2[7] are interesting for their diversity.

Some schemes were 'tweaked' and some were extended following their initial launch. Timing of schemes was set by each government, with the UK one of the last countries to launch its programme.

**Figure 2[8]; Car scrappage schemes; major EU markets**

<b>Germany</b>	14 January 2009 - 2 September 2009	Over nine years old	€2,500 to purchase a car up to 12 months old with Euro 4 as minimum engine specification – used car up to one year old. Total fund envelope €5 billion exhausted 2 September.
<b>France</b>	4 December 2008 – 31 December 2009	Over 10 years old	€1,000 to purchase a new car which is less than 160 g/km or an LCV.
<b>UK</b>	18 May 2009 – 28 February 2010– extended to 31 March 2010 or when fund is exhausted	Cars registered on or before 29 February 2000. LCVs up to 3.5 tonnes registered on or before 28 February 2002	£1,000 plus £1,000 from participating manufacturers – £400 million fund limit.
<b>Italy</b>	07 February 2009 - 31 December 2009	Over 10 years old	€1,500 - €5,000 to purchase a car which is at least Euro 4 engine specification and emits less than 140g/km for petrol and 130 g/km for diesel. Base €1,500 can be increased for cars running on CNG, electric or hydrogen. Base incentive of €2,500 for LCVs can be increased to €6,500 for vans running on CNG or €4,000 for vehicles running on LPG, electric or Hydrogen
<b>Spain</b>	1 December 2008 - 1 October 2010	Over 10 years old or 250,000 km	Up to €10,000 and 0% loan to purchase a new car or LCV. The car must cost less than €30,000 and emit less than 140 g/km. The LCV must emit less than 160 g/km. Also applicable to used cars up to 5 years old, providing scrapped cars at least 15 years old
	18 May 2009	Over 10 years old purchased new Over 12 years old purchased used	€2,000 - manufacturers pay 50% of incentive. New cars emit less than 149 g/km – new vehicle maximum €30,000. Applicable to used cars up to 2 years-old – maximum 200,000 vehicles

Source: ACEA/SMMT

Even the most sceptical observer must acknowledge that scrappage schemes have done their job of protecting full-year 2009 new car sales and production volumes from the crisis levels that were fast developing in the early part of the year.

### National scrappage schemes; a case study

*On the face of it Germany's was the most successful scrappage scheme*

On the face of it, Germany's was the most successful scrappage scheme. Total new car sales rose by 23.2% in 2009, the biggest jump since German reunification. The following points summarise the background, key elements and results of this programme.

- The January 2009 launched scheme was regarded as providing a much-needed boost for Germany's domestic new car market, particularly in the run up to a hotly-contested general election.
- The programme was heralded as a potential success quite soon after it started, and the fund was increased from an original €1.5 billion to a massive €5.0 billion.
- The scheme persuaded many car owners to take advantage of the special terms for scrapping their old car in exchange for a new car or a used car up to 12 months old.
- It paid out €2,500 per scrappage deal; old units had to be nine years or older.
- The entire scheme was paid for by taxpayer, so car manufacturers and dealers retained the flexibility to trade, offering additional incentives and the opportunity to make an acceptable margin on such deals.
- In August 2009, shortly before the scheme finished, the German scrappage scheme was reckoned to have lifted new car volumes by 28% compared with 2008. At the end of the programme in early September 2009 there were still 15,000 motorists wanting to participate.

The ability to recycle younger used cars, confidently and quickly, will also be seen as strategically supporting the car parc age profile and minimising longer-term implications of irregularities in the used car market.

*Tendency to buy smaller, lower-priced cars*

The challenge, as with any such scheme, was it tended to be the relatively better-off car owners who participated and, because of the sums on offer, there was a tendency to buy smaller, lower-priced cars.

Two challenges the Germans ably addressed from day one were – firstly, 'creating a scheme big enough to have a powerful impact on the new car market and be attractive' and, secondly, 'getting the scheme up and running quickly and well understood – so it made a big difference'.

## Widely voiced fear

There is now a widely-voiced fear in Germany that its scrappage scheme has perhaps been too successful, pulling forward new car sales that would have occurred naturally over the following two years or so, and accelerated sales of small, cheap and fuel-efficient passenger cars, and boosted imports dramatically.

The German new car market fell 26.6% to 294,375 units in March 2010 – standing 22.8% lower at 670,410 for the first three months of the year. The March drop reflects comparison with a very high base figure for 2009 when the German scrappage scheme was at its height – first quarter 2010 new car volumes are just 9% lower than those for 2008. However, double-digit declines are likely to become a pattern in Germany for much of 2010 as second and third quarter new car volumes fall well short of 2009's scrappage-driven results.

*Speculation that Germany's new car market could drop by around one million units in 2010*

There is speculation that the German new car market could drop by around one million units to around 2.8 million in 2010, largely because the scrappage scheme encouraged so many car owners who had no plans to buy a new car in 2009, to change their car anyway. Many of them will have been brought forward from 2010's potential car buyers, leaving fewer customers this year.

## Other countries' status

- The CCFA, the French equivalent of the SMMT, reported a 12.3% increase in new car volumes in 2009 compared with the previous year, the biggest year-on-year rise since 1990. French manufacturers also increased their share of the French new car market.
- The €1,500-plus per unit scrappage incentive in Italy has been particularly attractive to buyers of smaller cars; Fiat and Hyundai have done well.
- The Spanish scrappage scheme has also driven new car sales higher. Sales in December 2009 were 25.1% higher than December 2008. While fleet and particularly car rental sales were down in Spain, there was a near 48% rise in new car sales to private buyers. While overall sales were down by 17.9% for the full year in 2009, Spanish pre-scrappage new car volumes were running close to 50% below 2008 levels.
- An interesting comparison is Ireland, where no scrappage scheme was introduced in 2009. According to the SIMT, Irish new car sales fell by 62.1% in 2009 to just 57,457 units. An Irish scrappage scheme will run from 1st January 2010 to 31st December 2010, focusing on environmental performance, offering scrappage support up to €1,500 to motorists buying replacement vehicles with a CO<sub>2</sub> emission rating of less than 140gm/km.

There has also been a steady flow of Irish buyers to UK car auctions, reflecting the growing shortage of young, quality used cars in the Irish market and the favourable euro/pound exchange rate.

## The scrappage legacy?

Although scrappage schemes may have appeared good at the time, 2010 is now shaping up to be a really tough year for vehicle manufacturers. According to J D Power – ‘Overall western European sales are set to fall 10.5% to about 12.2 million in 2010, from 13.7 million in 2009.

*This is partly because the various scrappage schemes encouraged people who had no plans to buy new cars this year to do so anyway. Many of them will have been recruited from 2010's pool of car buyers, leaving fewer potential customers for 2010.*

*Another consequence of this is that manufacturers that gained the most from the scrappage scheme in 2009 are likely to be the ones that will suffer the greatest falls in sales this year – so makers of small cars may well be outperformed by firms making large or luxury cars in 2010. Similarly, countries that saw the greatest upswing in sales following the introduction of scrappage may see the sharpest fall in 2010. It may well be a story of the higher they climbed the harder they will fall’.*

*Countries that saw the greatest upswing in sales might see the sharpest fall in 2010*

IHS Global Insight takes a broadly similar view – ‘the German passenger car market is paying a heavy price in 2010 for the runaway success of the scrappage scheme. The 5-billion-euro fund benefitted the purchase of two million passenger cars and saw a year on year rise of more than 700,000 units. Now, the German passenger car market has to survive without further stimulus and a double-digit decline is pretty much what was expected following the massively high base created last year, with March, April, May and June 2009 posting particularly strong results.

*The Western European car market has now largely exhausted the various scrapping incentives, with the predictable effect expected in the coming months, as many markets begin to slide back to lower levels of activity. Western European car sales for the first quarter are now up 11% on 2009, but are now expected to reverse. The fragile nature of the recovery in many markets will see new car demand muted for much of the year, and will result in an overall fall of around 11% in the market in 2010.*

## Some initial conclusions

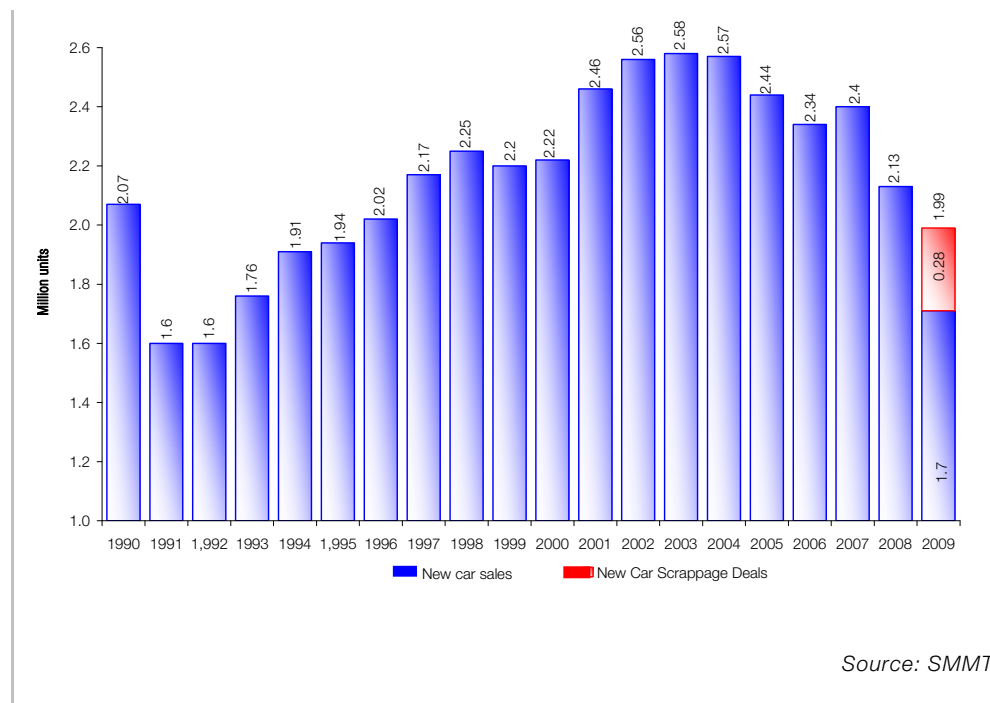
While European new car markets suffered greatly during the 2008 to 2009 recession, scrappage schemes have clearly had a mitigating effect on new car volumes, and nearly-new used cars in some markets. The longer-term consequences and benefits, or otherwise, of scrappage schemes will take some time to assess, although the question of ‘economic or political expediency’ might never be fully laid to rest.

# United Kingdom Automotive Industry

The UK automotive industry is unusual in that the bulk of the new cars sold are imported, while the vast majority of cars built in the country are exported. In the 1950s, the UK was the world's second largest car maker and premier exporter of cars, but has long slipped from this position.

United Kingdom new car sales peaked in 2003; falling markedly in 2008 and 2009 – Figure 3[1]. There is a growing acceptance in the industry that the aggressive approach of car manufacturers, and freely available credit, took new car volumes to around an arguably untenable 2.5 million units for something like five years.

Figure 3[1]; UK new car registrations; 1990 – 2009

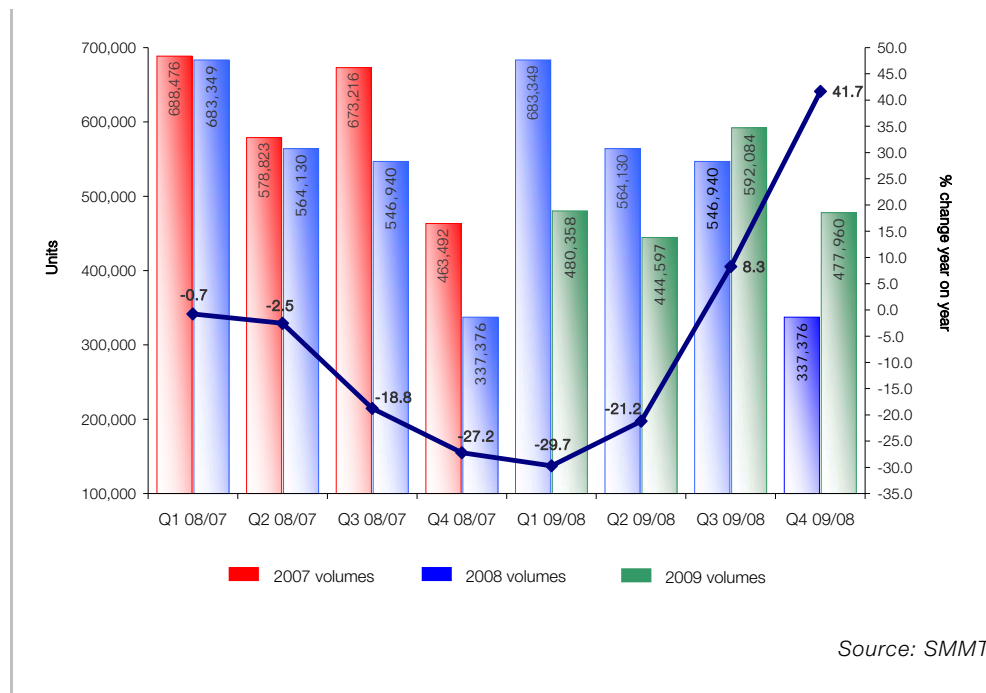


*Such a marked fall in new car sales happened very quickly*

As can be seen in Figure 3[2] overleaf, such a marked fall in new car sales happened very quickly. And, of course, the decline in new car volumes has to be seen as a ‘multiplier event’.

In the UK's mature automotive market, very few new car sales are truly incremental new car sales. Well over 90% of sales are replacement units which, in most instances, cannot take place until arrangements for the disposal of the existing unit are concluded. Thus, a new car sale is at the start of a ‘supply chain’ that nearly always places a used car in the market which, in turn, replaces another one – and so on.

Figure 3[2]; Quarterly UK new car registrations; 2007 – 2009



*The UK used car supply chain is far more influenced by new car sales that take place elsewhere*

Because such a high proportion of new cars sold in the UK are imported, the ‘supply chain multiplier’, in terms of manufacturing, is not as great as in most other countries. Indeed, the UK used car supply chain is far more influenced by new car sales that take place in Europe and elsewhere in the world.

Given the United Kingdom used car market is broadly three times the size of the new car market, and those used cars are already in use in the country, it is interesting that the government decided to focus purely on new car sales (over 80% imported) as its preferred way of stimulating the country’s car industry.

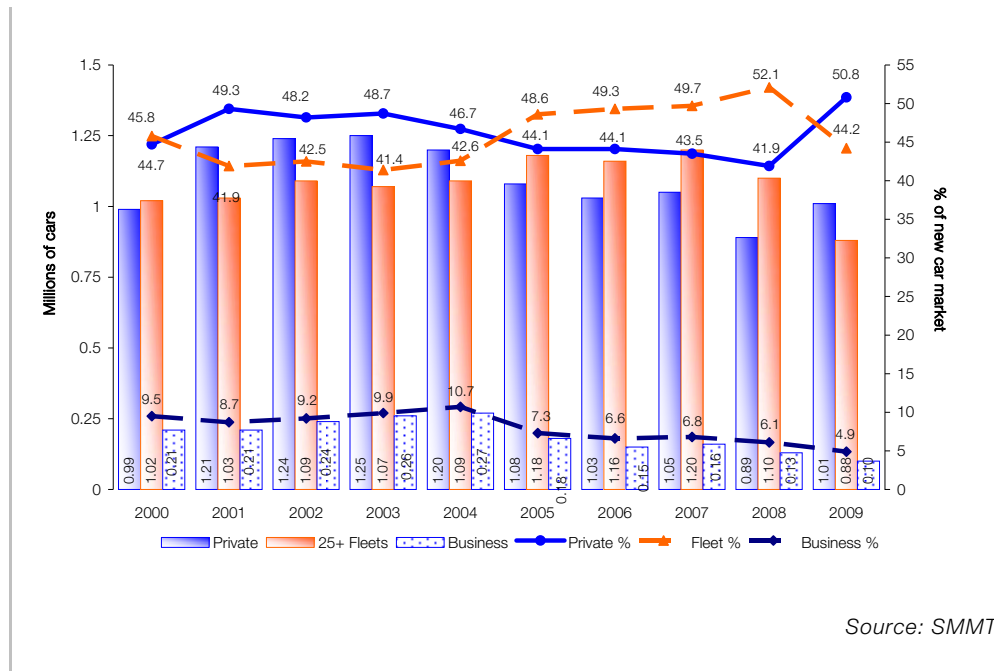
Indeed, any government incentive scheme aimed at aggressively building new car volumes will almost inevitably draw an arguably deserved jibe of – ‘supporting the Korean, Japanese and European motor industries – more than our own’.

### Recovery from recession

The symbiosis between the new and used vehicle market is often underestimated. Many would argue the two are separate markets, and private buyers will seek to change their used cars for younger used cars regardless of the state of the new car market.

However, given the used car industry is a continuum from second owner through to the oldest banger, a movement among buyers of the oldest, lowest-priced cars will have an impact right across the sector.

Figure 3[3]; UK Private, 25-plus fleet and business new car sales; 2000 – 2009



Source: SMMT

*New car sales to 25-plus fleets fell below the one million mark for the first time in many years*

New car sales to the 25-plus fleet sector in 2009 fell below the one million mark for the first time in many years, down 20.5% year on year to 882,415 units – Figure 3[4]. Many fleets extended their replacement cycle and/or cut their fleet size last year and, of course, were not party to the scrappage scheme – resulting in a quarter of a million fewer good quality cars reaching the used car market as a result.

Figure 3[4], UK new car market sectors

2009	Private	25-plus Fleet	Sub-25 Business
Registrations	1,014,304	882,415	98,280
% change 08/07	13.7	-20.5	-24.2
% market share	50.8	44.2	4.9

Source: SMMT

Of course, fleets cannot put off replacing cars indefinitely; the BVRLA believes 25-plus fleet new car volumes will top one million units once more in 2010. The latest SMMT forecast expects the new car market to drop to 1.817 million units in 2010, suggesting a substantial fall of around 200,000 units in private sector sales as the impact of the scrappage scheme wanes.

This is a view shared by Deloitte – *‘2010 figures will be affected by the impending end of scrappage, the increase in VAT and the rising input costs resulting from the fall in sterling. Our prediction is that there will be a dip in 2010 to around 1.7 to 1.8 million units, with the figures balancing out in 2011 to a long-term annual average of just under two million units.*

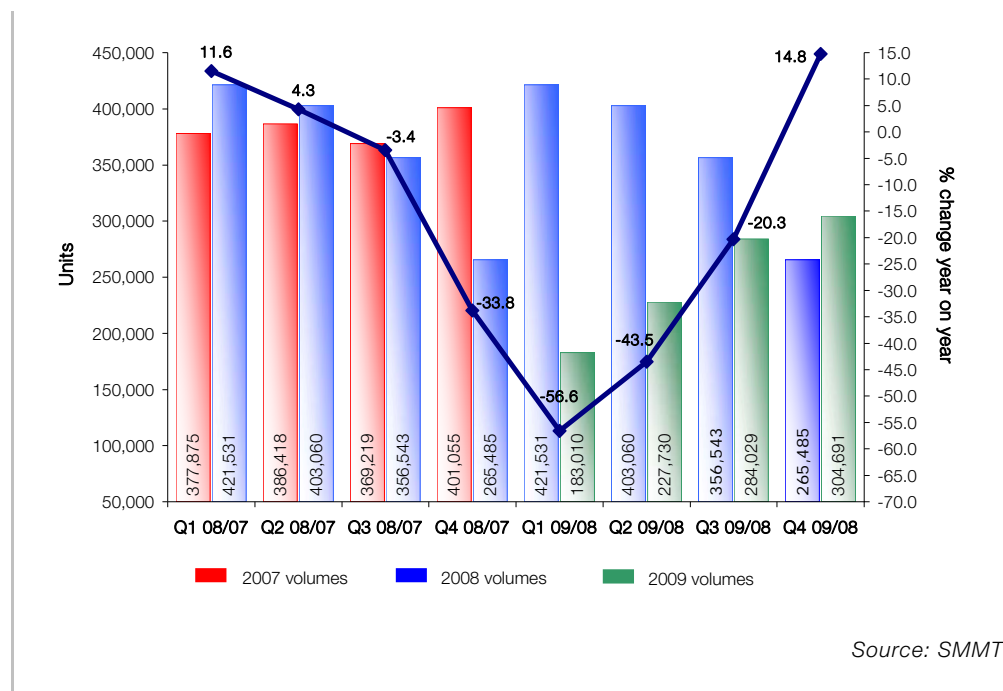
Only since the late 90s have we seen annual figures over two million units which many industry experts believe were due to additional registrations being forced on the market rather than due to consumer demand. The long-term average for the majority of the past three decades has been less than two million units per annum.

For the immediate future, it is unlikely we will return to the heady days of the past decade where unit numbers have been over two million. These numbers were unsustainable and a market correction has been expected for some time. Certainly over the short to medium term (3-5 years), annual new car registrations will remain sub two million’.

### UK car production

UK car production started to weaken in 2006; falling dramatically in the final quarter of 2008. Production continued in the doldrums during the first six months of 2009; output down by a half (414,000 units) on the same period in 2008. Although production volumes improved somewhat in the second half of 2009, they were flattered considerably by comparison with low volumes towards the end of 2008 – and remained well below 2007 levels.

Figure 3[5]; UK car production; 2007– 2009



*Car production – the lowest output for 25 years*

Figure 3[6] overleaf shows 2009 car production finished down 30.9% to 999,460 units, year on year – the lowest output for 25 years. Car production for domestic sales dropped 25.4% to 237,226 units last year, accounting for 23.7% of cars built in the UK. Production of cars for export also fell in 2009, down by 32.5% to 762,234 units; three quarters (76.3%) of UK built cars shipped overseas.

Figure 3[6]; UK car production; 2005 – 2009

	2005	2006	2007	2008	2009
<b>Total production</b>	1,596,356	1,442,085	1,534,567	1,446,619	999,460
<b>Home</b>	411,245	335,992	349,108	318,033	237,226
<b>% of total</b>	25.8	23.3	22.7	22.0	23.7
<b>Export</b>	1,185,111	1,106,093	1,185,459	1,128,586	762,234
<b>% of total</b>	74.2	76.7	77.3	78.0	76.3

*Source: SMMT*

With the sales of hundreds of thousands of small new cars pulled forward across Europe last year, there could be a stronger demand for medium and large models in 2010, as manufactured in the UK.

### Vehicle finance

In the same way that new and used car sales are closely related, so the availability of finance for vehicle purchase is a critical part of the equation. Figure 3[7] shows the substantial decline in new and used car Point of Sale finance advances in 2009. The former down 9% and the latter 11% year on year as new and used car volumes suffered in 2009.

Figure 3[7]; Point of Sale finance transactions 2009

	Value of advances £m		Number of advances 1,000s	
	New Cars	Used Cars	New Cars	Used Cars
<b>2009</b>	5,791	5,489	465	612
<b>% change vs. 2008</b>	-5%	-13%	-9%	-11%

*Source: FLA*

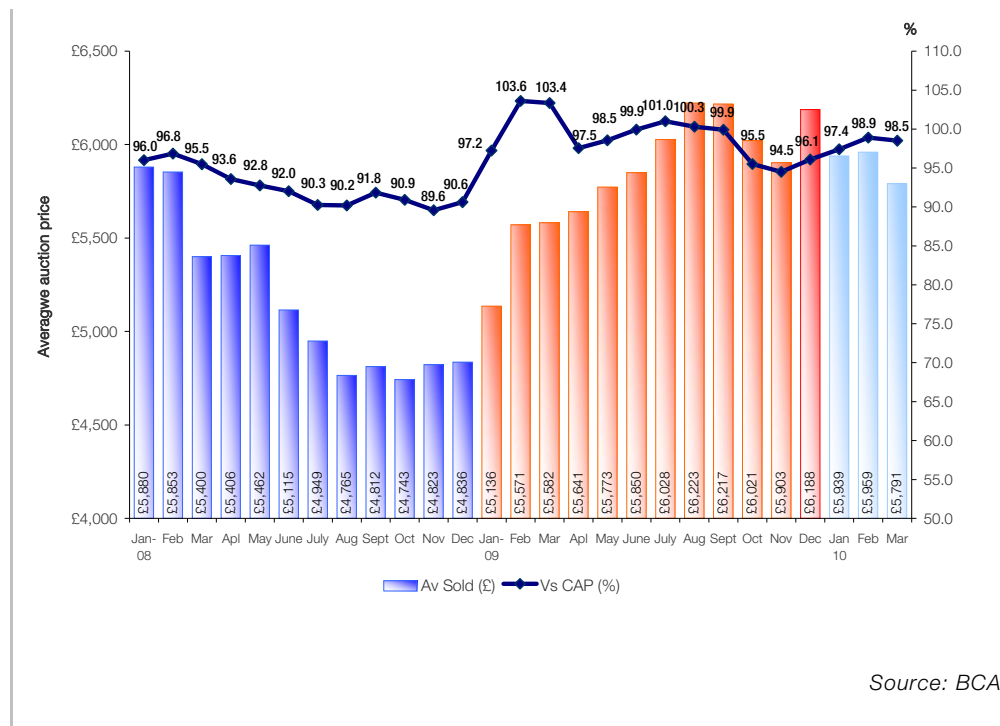
### Used car values rise in 2009/2010

Initially, average used car prices at auction were badly affected by the recession and plummeted during the second half of 2008 – recording a fall of over £1,000 for the year as a whole.

*2009 saw a strong recovery in used auction values*

- As new car volumes fell, 2009 saw a strong recovery in used auction values, remaining above the £6,000 mark for the July to October period – Figure 3[8] overleaf. While prices weakened somewhat in the fourth quarter, this follows a typical pattern of values peaking in September before falling slightly towards the end of the year.
- 2009 average prices finished £1,352 and 27.9%% higher year on year at £6,188. CAP Clean performance also recovered strongly in 2009, settling a few points either side of 100% for the first nine months of the year, falling back a little in the final quarter.

Figure 3[8]; Average used car auction prices; 2008 -2010



Source: BCA

- Much of the recovery in auction values reflects a shortage of used car stock during 2009, as dealers competed for a supply of good quality cars to retail.
- Price rises over a number of months – such as those seen in 2009 – are unlikely to be sustained, simply because the market had fallen so far and needed to recover. However, 2010 auction values remain slightly ahead year-on-year by £209 (3.7%) at the end of March, although this disparity has been reducing as values are now being compared to the recovering marketplace of 12 months earlier.

2010 auction values remain ahead year on year

### Some initial conclusions

This chapter has examined new and used car sales in the United Kingdom and shown how the new car market has dipped over the past four years. It has stressed that new and used car market sectors are closely linked and need to be treated together.

One issue, that will be examined later in the report, is that the new car sales decline seen in the past few years will have a direct impact on the wider automotive industry for many years to come, until the shortage of used cars has flushed right through the market – and that can only take place when a significantly higher volume of new cars enters the car parc in the first place.

It has also shown how resilient used car prices have been in the face of a deep and lasting recession.

# Scrappage, Implementation and its Legacy

## United Kingdom scrappage scheme

The United Kingdom scrappage scheme was, as some insiders have commented, developed somewhat reluctantly and late by government. It is almost unique, in European terms that car and van manufacturers have had to contribute half of the £2,000 scrappage incentive.

Figure 4[1]; United Kingdom scrappage scheme

<ul style="list-style-type: none"><li>• Passenger cars first registered in the United Kingdom on or before 29 February 2000.</li></ul>
<ul style="list-style-type: none"><li>• LCVs not exceeding 3.5 tonnes first registered in the United Kingdom on or before 28 February 2002.</li></ul>
<ul style="list-style-type: none"><li>• Vehicles to be scrapped and a new vehicle ordered.</li></ul>
<ul style="list-style-type: none"><li>• Participants to receive £2,000 incentive – £1,000 government incentive to be matched by £1,000 from participating vehicle manufacturers/dealers.</li></ul>
<ul style="list-style-type: none"><li>• Initial funding to last until 28 February 2010 was £300 million or until the fund was exhausted – sufficient to fund 300,000 replacement cars and LCVs. Extended to £400 million for 400,000 cars and LCVs in the same timeframe. On 4 February 2010, fund extended until 31 March or until £400 million fund was exhausted.</li></ul>
<ul style="list-style-type: none"><li>• The selling franchised dealer is responsible for administration, paperwork and for getting the vehicle scrapped in the right way.</li></ul>
<ul style="list-style-type: none"><li>• The scheme is inclusive of VAT.</li></ul>

*Source; SMMT*

*The programme was launched with strong support*

The programme was launched with strong support from vehicle manufacturers, the SMMT, the RMIF and other leading motor industry bodies in May 2009, with the scheme initially running to the end of February 2010.

While less generous than some European schemes, £1,000 of taxpayers' money was welcomed and has formed the basis of some high-profile sales programmes. During a period of deep recession, any programme with a significant external contribution to boost sales of new cars and LCVs must attract some plaudits. But, how does the UK scheme measure up to analysis?

### Scrappage – a qualified ‘Yes’?

The scrappage programme attracted a lot of positive headlines when it was announced. From a government point of view, it obviously helped create a ‘feel-good factor’, as new car volumes started to show improvement quite quickly, particularly compared with the dire monthly figures seen during the previous nine months or so. But, how does the UK scheme measure up to analysis?

Figure 4[2]; UK new car registrations percentage change year on year

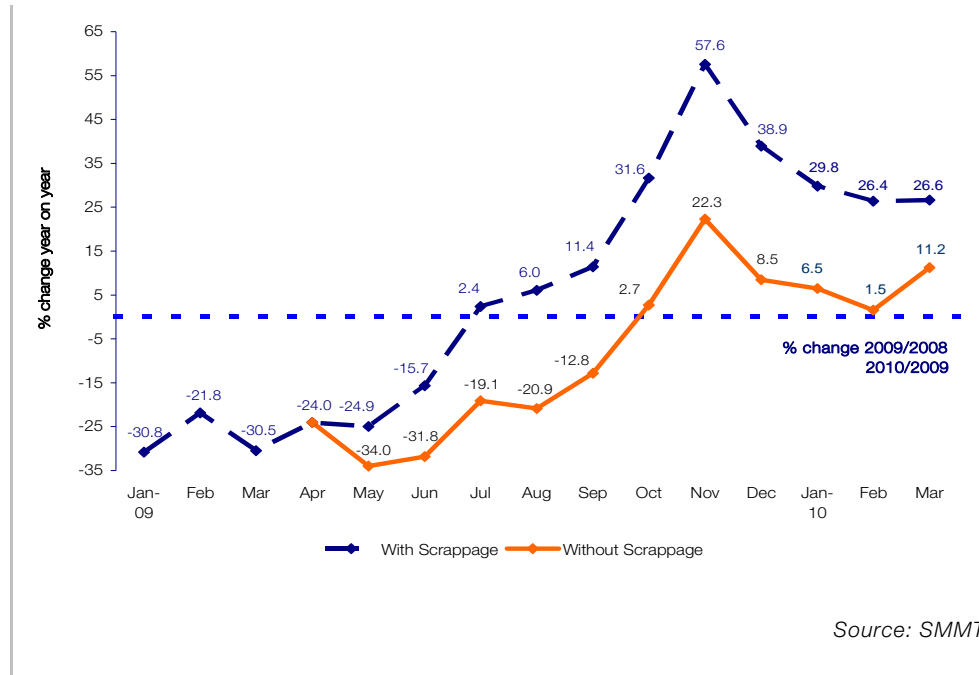
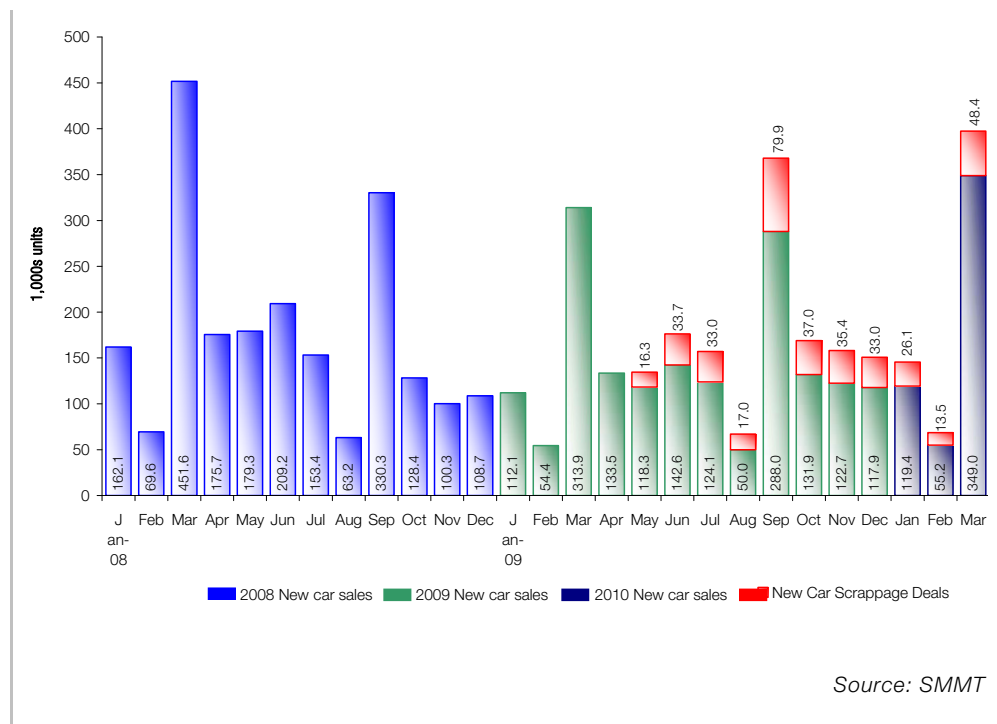


Figure 4[3]; UK new car registrations 2008 – 2010



From manufacturers' viewpoint, the outcome was encouraging as sales of new vehicles in the UK market improved. However, global manufacturers tend to look at markets in a less parochial way than governments. To a vehicle manufacturer, Europe is 'a single market block' and vehicles can be sourced from anywhere within the region or even further afield.

At a local level, scrappage has enabled manufacturers to rebalance their strategic and local vehicle inventories among their dealers. From dealers' viewpoint, the message is mixed. Scrappage certainly cleared the new car log jam to an extent, and it also regenerated interest in new car sales.

Funding half of the £2,000 scrappage incentive may have put some strain on dealers and manufacturers. At least part of the manufacturer/dealer contribution appears to have been funded by the withdrawal of price-based promotional plans, substantial new car price increases and less generous finance plans for new cars sold under the scheme.

### Cars sold through scrappage programme

*Many have been imported from Korea, Japan and central and eastern Europe*

According to the SMMT data on new cars sold under the scrappage scheme, many have been imported from Korea, Japan and central and eastern Europe where the proportion of UK-sourced components would have been pretty minimal.

Figure 4[4] overleaf shows 372,401 new cars were delivered under the scrappage scheme up to the end of March 2010, leaving a balance of about 20,000 orders to be delivered before the end of July to still qualify for the scheme.

With the prospect that the revised upper limit of 400,000 new car scrappage deals might not be reached before the scheme runs out at the end of February, the department for BIS announced the programme would be extended until 31 March 2010, or if the £400 million fund was taken up beforehand.

- The figures show the main beneficiary of the scrappage programme was Hyundai which sold 43,947 new cars under the scheme, accounting for 11.8% of total scrappage deals.

This compares with Hyundai's 1.3% of the new car market at the end of 2008 and 1.8% just before the scrappage scheme started – climbing to 4.2% for the first three months of 2010. Hyundai averaged 335 scrappage deals per sales outlet, 108 ahead of its nearest rival, Kia, with 227 per dealership.

- Other manufacturers taking a notably bigger share of new scrappage deals than their customary new car market share are Fiat, Kia, Mazda, Nissan, Skoda, Suzuki and Toyota.

Figure 4[4]; New cars sold under the UK scrappage scheme May 2009 – March 2010

Scrappage Deals May 2009 – Mar 2010				% New Car Market Share			
Manufacturer	Units	Share	Sales per Outlet	12 mths 2008	Jan-Apr 2009	12 months 2009	Jan-Mar 2010
Audi	4,298	1.2	37	4.7	5.2	4.6	4.9
BMW	3,706	1.0	25	5.3	4.4	4.9	4.1
Chevrolet	3,991	1.1	40	0.9	0.8	0.9	0.7
Citroen	9,958	2.7	51	3.8	3.4	3.6	3.4
Fiat	29,749	8.0	187	2.6	2.3	3.0	2.7
Ford	42,465	11.4	77	15.1	17.4	15.9	15.4
Honda	12,522	3.4	66	3.9	4.2	3.8	3.3
Hyundai	43,947	11.8	335	1.3	1.8	2.8	4.2
Kia	29,997	8.1	227	1.5	1.8	2.5	3.4
Mazda	11,280	3.0	71	2.3	2.4	2.4	2.4
Mercedes	1,830	0.5	14	3.5	3.6	3.6	3.3
MINI	6,563	1.8	44	1.9	1.6	2.0	1.8
Mitsubishi	2,214	0.6	19	0.7	0.5	0.6	0.5
Nissan	15,154	4.1	84	3.1	3.2	3.9	3.7
Peugeot	15,775	4.2	56	5.6	5.2	5.1	5.4
Renault	13,095	3.5	60	4.2	3.0	3.2	5.0
SEAT	6,639	1.8	61	1.4	1.4	1.5	1.6
Skoda	11,659	3.1	91	1.7	1.5	1.9	1.8
Suzuki	12,152	3.3	83	1.2	1.3	1.4	1.2
Toyota	27,950	7.5	149	5.0	5.4	5.1	4.7
Vauxhall	24,504	6.6	61	14.0	14.0	11.9	11.0
Volkswagen	29,678	8.0	135	8.4	8.3	8.1	8.4
Volvo	6,594	1.8	62	1.6	1.5	1.7	1.9
Others	6,681	1.8	37	6.2	5.8	5.4	5.3
<b>Total</b>	<b>372,401</b>						

*Source; SMMT/Buckingham*

- While Ford took second place in the table in terms of the number of units (42,465), its 11.4% share of scrappage deals is considerably lower than its new car market share before and after the introduction of the programme.
- With the exception of Hyundai, Kia, and perhaps Fiat, Toyota and Volkswagen, new car sales per outlet from the scrappage scheme have been modest for other franchises relative to their normal volumes – and would have had but a minor effect on job protection or dealer viability.
- Notable volume manufacturers who also ‘punched below their weight’ on the scrappage scheme are Peugeot, Renault, Vauxhall and Volkswagen.

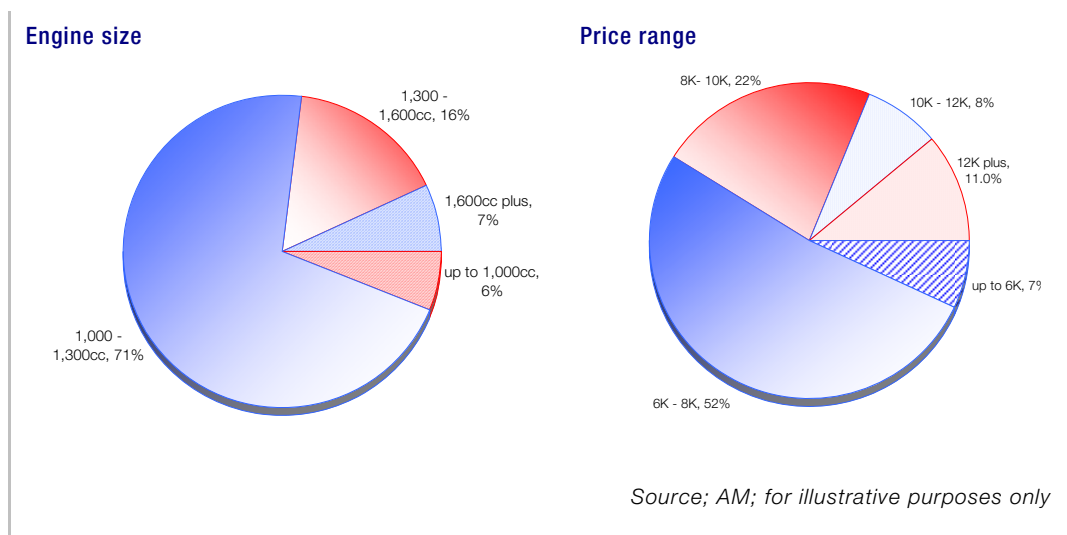
- New car market share figures shown in Figure 4[4] show that manufacturers that have benefited most from scrappage deals are also suppliers of smaller, lower-priced units, that may create a number of positive and negative strategic changes;
- Improved average fuel consumption; therefore reduction of the carbon footprint but reduced fuel tax take.
- However, there would be a greater logistics carbon footprint in terms of ‘finished vehicle mileage’ – from the Far East or CEE countries to the dealer.
- Change in distribution patterns with sales moving to ‘newer’ UK franchises away from longer-established franchised networks.
- Downsized vehicles supplied through scrappage are likely to have a lower service cost profile; extended warranty and longer service intervals eating in to dealers’ and independent service operators’ aftersales profitability.

### Scrappage and changing new car buyer patterns

While the UK scrappage programme may have provided a short-term boost to the new car market, it is interesting to consider ‘who has replaced their cars under the scheme?’

At the time of writing, there is a relative paucity of data in the public domain regarding car owners who have traded in their 10 year-old plus cars for new models.

**Figure 4[5]; Scrappage – new car replacement profile**



The data presented in Figure 4[5] is from an early sample of buyers from the UK scrappage programme, an interesting series of implications and potential conclusions had already begun to emerge;

- Prime beneficiaries bought ‘small, lower-powered, lower-priced cars’.
- Given a would-be beneficiary of the scrappage scheme has to have owned the car surrendered for at least a year – and because of the shortage of credit have access to funds, buyers will generally be established persons who ‘recognise a bargain’.
- Given the ‘owned for a year’ and ‘10 years old’ rules, by implication many of these vehicles could be lower-mileage runabouts – the image of ‘Auntie’s Morris Minor’ springs to mind.
- Developing the theme above, born out by anecdotal evidence, many cars being put to the crusher are often well maintained and in good condition for their age – offering further low-cost motoring, while some were future ‘heritage cars’ that have not been spared the crusher.
- Given these traded-in cars have to be scrapped, what will be the implications for the older used car market – private to private buyers – often the bailiwick of lower-paid workers who have no reliable bus or train to get them to work?
- Will the loss of up to 400,000 older used cars have a significant impact on service, repair, accessory and wider aftermarket sales? Would it be fair to claim many scrappage units would have been relatively well maintained, thus creating MOT and service business, part of which will now be lost in the longer service intervals of the replacement vehicles, initially covered by warranty?
- Given a significant clear out of older units, what might be the implications for used car prices – for the significant quantities of essentially entry-level new cars sold under the auspices of the scrappage scheme when they eventually appear for disposal, and also for the prices of older used cars?
- According to the Department for BIS, 60% of car owners who bought a new car under the scrappage programme were over 60 years old; 54% of all buyers had never bought a new car before, while more than half (56%) said they would not have bought a car at all at this time if the scrappage scheme had not been available.

*Many cars being put to the crusher are well maintained and in good condition*

*What might be the implications for used car prices?*

While such ‘Miss Marple-like images’ might be wide of the mark, and entirely speculative, it raises issues for the longer-term impact of the scrappage scheme.

### **The used car issue**

Unlike the German scrappage programme, the UK programme only covers new cars and LCVs. Thus, a real problem has been created for dealers in terms of the natural demand for used cars.

Many buyers, up to 400,000 units, have been taken out of the used car market. It would not be a step too far to claim that it is highly likely that a significant number of the 'scrappage scheme beneficiaries' would normally have bought a used car at some point in time, maintained it and replaced it after a few years.

*The used car buying opportunity will probably have been lost for several years*

With a car replaced under scrappage, that used car buying opportunity will probably have been lost for several years, particularly if the replacement unit is covered by a five year, or more, warranty. Many older people, who have bought a new car for the first time under the scrappage scheme, will possibly plan to keep it for as long as they continue driving.

### **Vehicle finance**

It is generally accepted that one of the principal issues with both new and used car sales in the United Kingdom has been the lack of vehicle finance. Indeed, many dealers would claim this has been one of their biggest problems during 2008-2009.

Car manufacturers' finance houses making finance available for scrappage schemes could be claimed to be one of the reasons for the programme's success. Manufacturers' finance houses have offered a major lifeline in the marketplace, but that funding has often focused largely on new vehicles. As a result, there has been a significant shortage of funding for used cars which, in turn, helped drive down used car sales and prices in 2008. This will need to be addressed once scrappage programmes come to an end.

Longer-term implications are that a lack of funding for used vehicle acquisition could also slow down new car sales. Most buyers need to be able to release the equity in their current vehicle before they are able to buy a new one.

If these funds are not available further down the supply chain, the whole process slows down considerably. While this might be considered an unintended consequence, it illustrates yet again the relationship between new and used cars and the reality that we are working with a continuous supply chain. If one element is affected, those behind it will stop or slow down too.

### **The end of scrappage – where next?**

*The end of scrappage may leave many private motorists to contemplate whether they should replace their car*

The end of scrappage deals may leave many private motorists to contemplate whether they should replace their cars – or not. Given the rise in VAT to 17½% from beginning of January, price hikes in fuel and fuel duty increases in the pipeline, as well as producer price increases and currency concerns, not to mention higher VED and first year registration fees for new cars, private motorists may well decide to defer their car replacement. The impact could be a sizeable drop in private buyers and a significant hit on dealers' sales and profitability for some considerable time to come.

## Scrappage – some early conclusions

The number of new car and LCV scrappage scheme orders was close to 400,000 at the end of March 2010 – of which 378,978 were delivered before the end of March. Under the rules of the scheme, the outstanding orders must be delivered by the end of July to qualify for the £2,000 scrappage incentive – boosting new car registrations over that period.

At its outset, the UK scrappage scheme aimed to drive up UK car and van sales and protect jobs in vehicle manufacturing and its supply chain, at a time when sales and production were both nearing crisis levels. It was also intended it would benefit the automotive retail sector in terms of higher new car volumes, as for example in Germany, and more importantly, profitability.

The full results and impact of the car scrappage scheme will take some time to emerge and be fully evaluated. However, at this stage, the Buckingham Automotive Team believes the following points are both relevant and important;

- The scrappage scheme has been heralded as a great success in many quarters for its contribution to the motor industry since its introduction. But, does it truly live up to its aims and the Department of Business, Innovation & Skills' assessment? Commenting on the scheme's closure, business secretary Lord Mandelson said, *'The scheme was always time limited and today as it closes I am pleased to see scrappage has delivered the results we aimed for – not just for manufacturers, but for the whole industry and its supply chain. The figures show that this scheme gave vital support, boosting demand when the industry needed it most, helping to position the auto sector to meet the challenges of building a strong low carbon future'*. A view very much shared by Paul Everitt, the SMMT's chief executive – *'The Scrappage Incentive Scheme has given a much needed stimulus to the UK motor industry boosting sales and production volumes, protecting thousands of jobs in retail and manufacturing'*.

**Costs;** the cost of the scrappage programme was shared equally between the government (taxpayer) and vehicle manufacturers/dealers – each contributing £1,000 to the £2,000 incentive on each deal – close to £400 million in total for each of the parties.

- From the government's point of view, the scheme is likely to have been self financing taking VAT contribution into account. While an average price for new cars bought under the scheme is not available, the government would have broken even at a sales price of £6,666.66 when VAT was 15%.
- The Department of BIS has yet to publish the average sales price or the total amount taken in VAT under the scrappage scheme. However, it appears that around three out of 10 cars bought under the scheme were larger than the Supermini segment, leading to speculation that the average unit price could be closer to the £8,000 mark.

*The cost of the scrappage programme was shared equally between the government and manufacturers/dealers*

If that were the case, the Treasury would have reaped about £350 million in VAT (15%) from the vehicles sold under the scheme between May and December last year – and a further £150 million from the balance of deals up to the end of March at the higher rate of 17.5% – an upfront ‘profit’ of around £100 million for the Treasury.

*The costs of the scheme would exceed benefits and would not provide value for money*

- The National Audit Office’s (NAO) view was *‘In the longer term, the costs of the scheme would exceed benefits and would not, therefore, provide value for money. The Treasury will reap a short-term gain of £116 million, but a long-term loss in the region of £18 million. The estimated long-term loss is principally due to a prediction that some 54% of sales would occur anyway, rising to 92% in the long term. Also, some 85% of vehicles sold in the UK are imported, although the UK is likely to have benefited from exports to other countries running similar schemes and many components are made here’.*

**Vehicle manufacture;** looking at the chart in Figure 3[5] shows car production made a significant recovery in the second half of 2009 from the dire levels of the previous nine months, that were typified by short-time working at several plants and Honda’s factory closure.

But, how much this was due to the UK scrappage programme and how much to scrappage schemes in Europe is, of course, open to debate.

- While the number of UK-built new cars sold under the scrappage programme has not been released, it is clear that the vast majority have been imported from Europe or wider afield. A quick look at the table in Figure 4[4] suggests that around 85% of new cars registered under the UK scrappage scheme were imported – close to 30% of the total from the Far East – although there is speculation that the imported figure is closer to 90%. It is likely, therefore, that only 37,000 to 56,000 of these new units will have come from a UK plant – a fraction of a normal year’s passenger car output.
- While some of the imported cars would have been built with engines made in Britain, few of their other components would have been manufactured here – risking comments that the vast majority of ‘taxpayers’ money invested in the scrappage fund has been used to support other countries’ car manufacturers and their supply chain’.
- Arguably, such a very small amount of home-produced cars from the UK’s scrappage programme is not the panacea for UK car production that some have claimed. It appears that protecting thousands of jobs in the country’s car and engine production, the supply chain and distribution networks, has been delivered far more by judicious short-time working, factory shutdown, redundancy programmes and other cost-cutting measures introduced by manufacturers – and, of course, the many orders for UK-built cars generated by other European countries’ scrappage schemes.

*Many orders for UK-built cars generated by other European countries’ scrappage schemes*

- A view that is supported by KPMG – *‘Although we have seen a significant improvement in new car sales in the UK over the last few months, vehicle production in the UK is still declining with car production down 31% on the prior year and commercial vehicle production down 55%.*

*The principal reason for the discrepancy between recovering UK sales and declining car production is the scrappage scheme. Although the scrappage scheme has provided a much needed boost to the retail sector, the vast majority of cars sold under the scheme (over 90%) are imported vehicles and, as such, has provided no meaningful benefit to UK manufacturers and component suppliers. Indeed the majority of cars assembled in the UK are destined for export markets and, it is not until there is a sustained improvement in global markets, will UK car production recover.*

**Retail sector;** clearly, the scrappage scheme has been a powerful stimulus as far as new car volumes are concerned, tempting many more private new car buyers into the market during a period of recession.

- The scheme has helped build confidence in the automotive retail sector, heightened new car and dealer visibility and brought up to 400,000 mostly new customers into the franchised dealer arena. It could be argued it has also produced a feel-good factor that has benefitted the motor industry and a considerable short-term political payback for the government
- The majority of new cars sold under the umbrella of scheme have been to motorists who wouldn't ordinarily buy a new vehicle. In normal circumstances, these owners of older cars would likely buy a used car at some point, triggering one or more sales up the used car supply chain until someone bought a new car – over time generating more aftersales and finance business for the retail sector – probably more than a million transactions.
- It must also be acknowledged that most new cars bought under the auspices of the scrappage scheme are lower-priced models offering lower profit opportunities – no part-exchange to retail – little or no finance contribution – little opportunity of immediate aftersales business – or the likelihood of the car entering the used car market in a normal replacement timescale.
- While on a wider front, there seems to have been fewer dealers going out of business than might have been expected during a lengthy recession, this is probably a lot more to do with sensible management and tight cost control than a substantial ‘bottom line’ profit contribution from new car scrappage deals.

*In normal circumstances, these owners would likely buy a used car at some point in time*

# Sustainable Recovery and Strategic Development

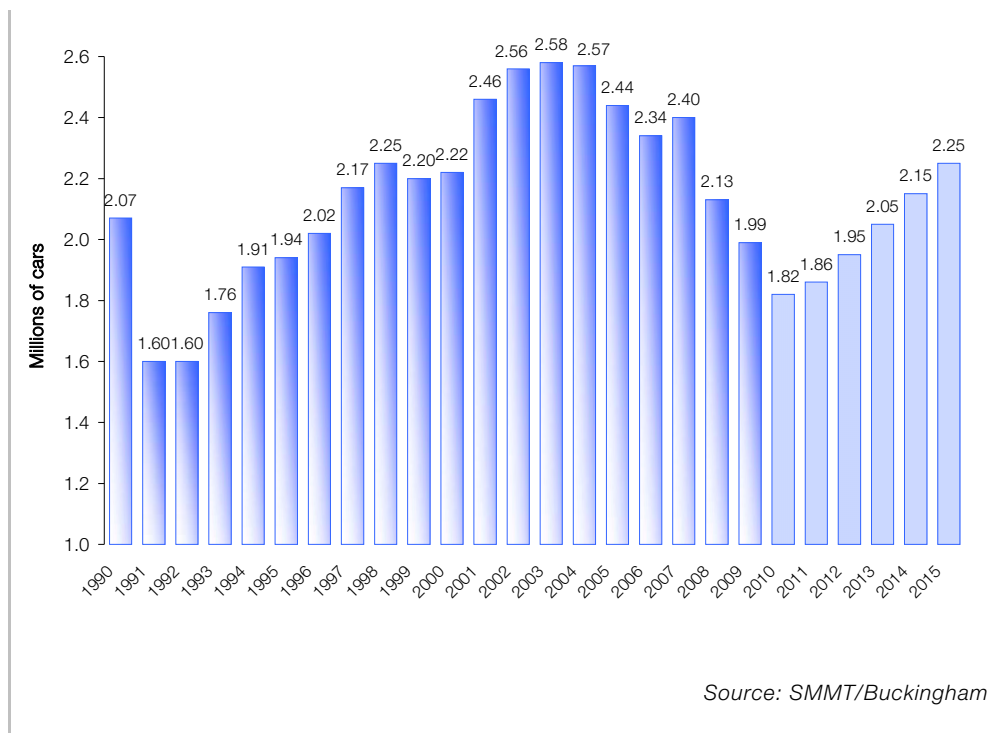
Previous chapters have examined the effect of the recession on car sales in the United Kingdom and the impact of the taxpayer part-funded scrappage programme. The impact of the recession on the retail motor industry is likely to last for over 10 years and the scrappage programme will also influence the future shape of the industry.

*If scrappage deals are excluded, the natural market was close to 1.7 million units last year*

New car sales from the scrappage programme helped lift the UK new car market to some 1.99 million in 2009. But, if the scrappage deals are excluded, the ‘natural market’ was close to 1.7 million units last year. As the economy recovers from recession, so the scars from much lower new car volumes over the period 2006 to 2012 and beyond, will have a significant and lasting impact on the entire industry.

Figure 5[1] shows historic new car sales and predictions through to 2015. A number of commentators believe these forecasts are somewhat optimistic and that UK new car volumes could well settle around two million units for several years to come.

**Figure 5[1]; UK new car registrations; 1990 – 2015**



Importantly, the current practice of focusing on high month-on-month percentage rises in new car sales and production, versus the previous year’s low base, should not be allowed to camouflage that 2010’s new car sales are currently expected to be the lowest since 1993.

Certainly one might expect a degree of 'catch-up', as fleet operators and leasing companies seek to rebalance their fleet profiles despite higher prices and longer lead-times. This catch-up will also mean a growth in higher mileage used cars – the 100,000 to 110,000 mileage band of nearly five year-old units.

This flushing through of older used company cars may also have implications for used car prices at auction, in terms of changing the mix of used cars offered for the first time to the used car market. There may also be a level of downsizing driven by companies' green agendas and changes in the taxation associated with company cars and higher fuel prices.

### Impact of recession and scrappage on the UK car parc

The euphoria of improved car registrations in the United Kingdom, particularly towards the end of 2009, with December recording a 38.9% improvement versus a low output in the same month in 2008.

UK new car sales for January to March 2010 also seem promising at first glance, posting a rise of 27.3% compared with the recession-driven first three months of 2009. But, without 87,932 scrappage deals, 2010's new car volumes for January to March would have been 523,616 – 23.4% and 160,033 units fewer than the corresponding period two years earlier in 2008.

*UK new car sales for January to March 2010 also seem promising at first glance*

As mentioned earlier, the UK new car market is expected to be around 1.8 million units in 2010 – the lowest since 1993. The concern felt by the team at the Centre for Automotive Management is the impact the recession and a prolonged period of low new car sales will have on the new car market and the country's car parc.

- **New car mix;** recession has caused many fleet operators to delay replacing cars. Many leasing companies have seen contracts extended to five years and over 100,000 miles. These fleets are now starting to reorganise their car requirements and business needs that, in part, is showing through smaller fleets and vehicle downsizing. This trend is expected to continue.

Private buyers also appear to be downsizing and the scrappage scheme has led to around 400,000 older vehicles being taken out of the car parc and replaced largely by smaller cars. Immediate effects from the change in car parc mix driven by recession and scrappage include;

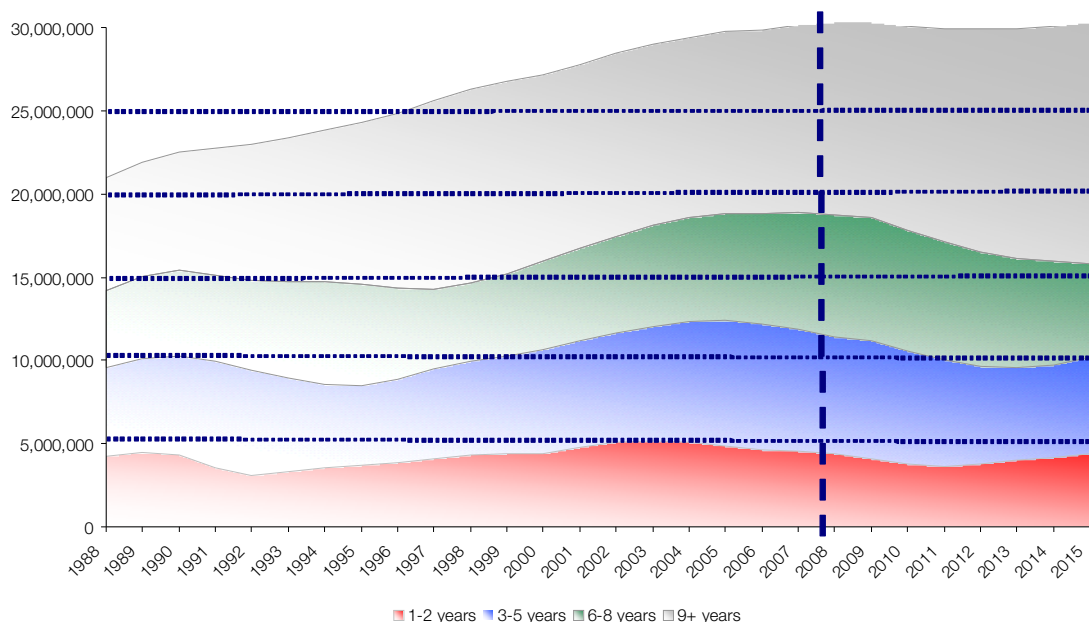
- New car sourcing – a growth in smaller cars – often from the Far East, often with low service requirements and high warranty thresholds.
- Reduced number of new cars being acquired.
- Change franchises from which these vehicles have been acquired

While small initially, these issues could become significant over time.

- **Evolving car parc;** a sustained sharp decline in new car sales means, over time, there will be an ageing of the total car parc.
  - There has been a marked decline in the new car market since 2005 which has led to a substantial change in the age mix of cars in the parc.
  - Historically, franchised dealers have traded predominately in the cars up to about five years old. To that age, they can generally sell the new car, sell the vehicle as a used car and also capture a decent share of the service and repair business associated with these younger units.

Figure 5[2] has been developed by the CAM team predicting the likely volumes of cars in the various age categories.

**Figure 5[2]; UK car parc to 1988 – 2015 by age groups**



Source; Buckingham; for illustrative purposes only

The size of the 'younger car parc' is now declining fast due to the huge fall in new car volumes since 2008. Currently, from a franchised dealer's viewpoint, it does not matter if older units are retained longer as, traditionally, that is not a pond they have fished in. Interestingly, Pendragon has confirmed it had moved from traditional stocking of three to four year old used cars and is targeting the older used car market as a key area for growth.

*The steep fall in new car sales will have an enormous impact on the UK car parc*

The steep fall in new car sales in 2008/2009, and the sluggish recovery expected, will have an enormous impact on the UK car parc. The overall car parc will fall by less than half a million units over the next three years before starting to grow again in 2013 – although the average age and mix of the car parc will change radically.

There were 12.4 million 0-5 year-old cars on the roads at the end of 2005, falling to 11.4 million by the end of 2008 – and to around just 9.5 million by 2013 – growing slowly, thereafter, as hoped-for, higher new car volumes eventually feed through to this age sector of the parc.

*Posing a serious threat to used car stock availability and used car volumes*

For used car retailers, who deal primarily in younger used cars (0-5 years old), there will be around three million fewer of these units ‘in stock’ by 2013, than the high point of 2005 – nearly two million fewer than the 2008 figure – posing a serious threat to used car stock availability and used car volumes in this age group over the next few years. *(see Recession and Recovery; A Strategic Analysis of the Used Car market – a report for BCA by The Centre for Automotive Management at The University of Buckingham)*

### **‘Black hole’ in the aftersales market**

It is also not difficult to work out the implications for the size of the service/repair market – or the huge task that dealers face to sustain their aftersales business. If there are substantially fewer cars on the country’s roads for any age group, then service and repair market for that sector drops accordingly – there is no way of producing units magically to fill the gap.

*There is a ‘black hole’ looming in the aftersales market for younger cars*

There is a ‘black hole’ looming in the aftersales market for younger cars – amounting to around £2 billion in the 2009 to 2015 period compared to 2008’s level – at its worst between 2012 and 2014. *(see Recession and Recovery; A Strategic Analysis of the Used Car market – a report for BCA by The Centre for Automotive Management at The University of Buckingham)*

The challenge now – is what do car manufacturers, franchised dealers, used car retailers and independent service outlets, as well as the support companies, do to modify their business models to take account of the significantly smaller and slow to recover parc for younger cars.

### **Knock-on Implications**

Quite simply, the market that franchised dealers, in particular, operate in is changing; scrappage and the economic recession and market dynamics have and will continue to change the shape and magnitude of the market.

Lower-cost new cars, fewer of them and a shrinking younger used car parc will all contribute to a much tougher, more competitive market.

Consider some of the knock-on implications;

- Contraction in vehicle parc and the vehicle base that dealers rely heavily on for their service business and used car activities.
- Potential shortage of younger used cars for some years may force up used car prices to rebalance the market.

- Significantly less aftermarket business available for franchised dealers and service specialists in the younger car age bracket.
- Car parc mix changed unnaturally by 400,000 older cars replaced under scrappage – the majority of which are small cars.
- Reduction in routine service and repair opportunities for dealers caused by extended warranty and longer service intervals of cars replaced under scrappage.

A counter argument might be that the dynamics of the car parc will change with the older vehicle units and buyers will simply retain their cars longer and still have them maintained. From the franchised dealer viewpoint, that may mean a different problem – will owners be willing to pay franchised dealers' hourly charge-out rates for service on old cars, which appear extraordinarily high compared with the residual value of the car – or will they look for alternative, lower-priced service facilities offered by the independent sector?

*The clear message is change the dealer business model*

Other knock-on effects may be readily identified – the clear message is 'change the dealer business model or expect a marked contraction in business'.

### Car manufacture activity

In recent years, manufacturers have employed a number of tactics to build market share in what may, with hindsight, have been a declining market. Perhaps, the routes taken, have been the most expensive – 'heavy discounting' or 'cheap finance' and/or various packages to cut the perceived price.

The checklist in Figure 5[3] highlights some of the broad strategic issues that might be considered;

**Figure 5[3]; Car manufacture market development checklist**

- Ensure there is a competitively priced finance house programme in place for new and used car buyers.
- Offer dealers opportunities to acquire ex-company cars to refurbish to their local market standards and requirements.
- Offer franchised dealers appropriate opportunities for used vehicles – ensure the requirements are not onerous.
- Provide support if necessary for franchised dealers to develop their used car activities.
- Advise, don't order dealers to follow specific sales and marketing programmes.

*For illustrative purposes only – not comprehensive*

While the manufacturer support is seen as pretty basic, dealers are ultimately responsible for car sales; they know their local market.

### Possible dealer actions – a new dealer approach?

Dealers, too, will need to come to terms with the changing market they operate in, and the fact it will contract on a number of fronts over the next few years. There are a broad range of actions dealers might consider to protect themselves from this drop in their traditional market.

Consider the checklist shown in Figure 5[4]; the objectives are two-fold – create and sell more added-value and secondly take share from competition while retaining margins;

**Figure 5[4]; Checklist; dealer development in a recovering market**

- Downsize strategically the dealership to reduce the cost base to reflect lower profitability.
- Review business model and staffing – are there strategic cost reduction opportunities?
- Consider seeking additional complementary market franchises.
- Expand into new market segments – particularly those not requiring additional vehicle sales but enhancing profit opportunity.
- Develop new value-added services – e.g. daily rental and leasing activities.
- Review used car operations, market segmentation and associated marketing activities.
- Seek alternative sources of Point of Sale finance so new and used car customers can be matched with competitive buyer finance.
- Ensure staff are suitably trained, motivated and monitored.

*For illustrative purposes only – not comprehensive*

While none of these points could be called rocket science, not all businesses pursue them all.

### Used car activities

The market analysis outlined earlier in this chapter suggests changes in the profile of the vehicle parc and the used car market. It is important dealers and car manufacturers review the used car sector and sourcing to ensure dealerships have the relevant quality used cars for their target markets. Consider the following checklist;

**Figure 5[5]; Used car activities in a recovering market**

<ul style="list-style-type: none"> <li>• Review the used car profile and the market segments the retailer will operate in to ensure it is large enough.</li> </ul>
<ul style="list-style-type: none"> <li>• Determine refurbishment strategy and appropriate cost levels.</li> </ul>
<ul style="list-style-type: none"> <li>• Develop used car sourcing to ensure up to date inventory – auctions, direct deals from leasing companies etc.</li> </ul>
<ul style="list-style-type: none"> <li>• Used car presentation.</li> </ul>
<ul style="list-style-type: none"> <li>• Target market groups and appropriate means of communicating with those groups.</li> </ul>
<ul style="list-style-type: none"> <li>• Used car funding for clients.</li> </ul>
<ul style="list-style-type: none"> <li>• Inventory strategy and disposal strategy for over age units.</li> </ul>
<ul style="list-style-type: none"> <li>• Ensure all channels for profitable stock procurement are used</li> </ul>
<p><i>For illustrative purposes only – not comprehensive</i></p>

While, once more, none of these actions can be called rocket science and are, in truth, back to basics, it is critical that used car retailers review and implement professional programmes to gather incremental business.

### **Some initial conclusions**

The shape of the car parc is changing and will continue to change over the next few years. There will almost certainly be fewer dealerships and secondary service providers. It is important dealers plan how they will exploit the evolving, smaller and more competitive market – ‘more of the same’ is clearly not the answer.

# Implications and Conclusions

The foregoing chapters have sought to spell out a picture of a dynamic United Kingdom automotive sector – one that is subject to sales fluctuations and dramatic changes that will take something like a decade to flush through the system until the effects of recent recession recede.

While some commentators might consider scrappage to have been a political expedient to create a ‘feel-good factor’ – that has stimulated largely foreign-manufactured new car sales – it has also provided a welcome boost to volumes, if not profitability, for car manufacturers, dealers and some service providers.

On the assumption the UK economy is now at the start of a long-term, sustainable economic recovery, the motor industry and dealers may well be advised to review their business models.

While, historically, credit was easily available to buy new or used cars, it will, at least medium term, be in tight supply. Sales of new cars are likely take some years to return even to a sustainable two million units per year mark. To support these and the associated sales, against the background of an ageing car parc, with cars creating less service opportunities – longer service intervals and downsized vehicles - there will be significantly less traditional franchised dealer business available.

*Sales of new cars are likely to take some years to return to a sustainable two million units per year mark*

The message to used car retailers is ‘review your business model’ identify new business opportunities – perhaps change the age profile of used vehicles sold; become more professional at used car marketing; seek and develop new, ‘soft’ business opportunities – or consolidate or shrink the size of the business to survive and prosper.

Management during recession, the knock-on effects of scrappage and nurturing of sustainable recovery will demand a much different, holistic and professional business model.

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