Goodman
The Response Agency

Automotive industry market report

Overview

The New Car and Light Motor Vehicle Dealers industry has grown strongly over the past five years. Cheap finance deals, the wider availability of new technologies in new cars and the improved fuel economy offered by new models have all contributed to the industry's strong performance.

However, falling consumer confidence and business capital expenditure due to prolonged uncertainty caused by ongoing EU exit negotiations have constrained growth in the current year.

Recent industry figures

New car registrations fell for a third consecutive month into June 2017, after increased sales at the start of 2017 as customers brought forward purchases to avoid increased Vehicle Excise Duty (VED) charges that took effect in April 2017. Industry revenue is estimated to grow at a compound annual rate of 3.8% over the five years through 2017-18 to reach £125.9 billion, with a marginal growth of 0.9% in the current year.

Industry profit margins fell over the past five years due to increased purchase costs from car manufacturers, as a result of the depreciation of the pound in 2016-17. Additionally, competition from online sales have weighed on profit margins, and profit is expected to account for 7.2% of industry revenue in the current year.

At the start of the period, demand was affected by subdued economic activity and relatively low consumer confidence as well as static business confidence. This prompted many businesses to limit expenditure and postpone purchases of new cars, with some companies opting to lease instead.

Later in the period, sales improved considerably in line with economic conditions and new car sales have grown for five consecutive years in the United Kingdom. New car registrations increased for 43 consecutive months until a 1.1% fall in December 2016, according to the Society of Motor Manufacturers and Traders (SMMT).

A combination of increased car prices and registrations led to an estimated 10% increase in industry revenue in 2014-15. Industry revenue has continued to grow, with registrations reaching 519,000 in March 2016, the second highest month ever for new car sales. Additionally, the continued availability of financing deals and rising household disposable income resulted in high demand for new cars.

The six months through June 2016 had the highest ever number of registrations in a six-month period, which contributed towards a record 2.7 million cars being registered in 2016. However, new registrations grew by just 0.1% in July 2016, the month following the EU referendum. Revenue is expected to grow only marginally in the current year as new car sales fell for three consecutive months prior to June 2017, according to the SMMT.

Constrained household budgets due to rising inflation and weak wage growth, compounded by uncertainty surrounding the United Kingdom's future relationship with the European Union, offset record sales at the start of the year.

Trends

The success of dealerships in recent years has been attributed to a variety of factors, including low unemployment, rising discretionary spending, and rising fixed investment levels. Demand has also grown thanks to the increased availability of cheap car finance deals. These deals include hire purchase and personal contract plan arrangements, which allow consumers to split payments into more manageable monthly instalments, avoiding the large initial capital outlay involved in purchasing a car outright.

For private individuals and small businesses that buy light vehicles, purchasing a car is more attractive when it is advertised as having low monthly payments. New technologies and improved fuel economy have also encouraged consumers to buy new cars, because running costs are lower.

Alternatively fueled vehicles

Alternatively fuelled vehicle sales have increased significantly over the past decade and it has been the fastest growing product segment in recent years, but AFVs account for a small proportion of industry revenue. The most popular AFVs are hybrid electric vehicles, which had a 25.3% increase in new registrations in June 2017 compared with June 2016. Plug-in hybrids are next most popular AFVs, and registrations increased by 33.8% in June 2017 compared with June 2016, according to the SMMT. The number of vehicles eligible for the plug-in grant has grown as customers have taken advantage of government initiatives.

AFVs typically use less fuel and emit less greenhouse gases than conventional vehicles powered by internal combustion. The sales of electric cars and AFVs have slowed in the current year in line with overall sales, due to economic uncertainty. SMMT data shows a 1.3% decline in new registrations of electric and AFVs for the year through June 2017, compared with the previous year.

Sales of plug-in vehicles are expected to grow over the next five years. This includes plug-in pure electric cars and hybrid cars. The government has introduced several policies to encourage the further penetration of electric cars into the mainstream market. The Plug-In Car Grant scheme, which has been extended to 2018, offers consumers up to 35% off the price of a plug-in vehicle. These vehicles are usually ultra-low emission vehicles (ULEVs) that produce less carbon dioxide. The government announced plans in 2017 to ban sales of all new diesel and petrol cars and vans by 2040. This means the future growth of the industry is solely based on AFVs and electric vehicles.

Other campaigns, such as *Go Ultra Low*, a joint government and car industry scheme to encourage motorists to switch to electric vehicles, have been successful at encouraging private and commercial demand for these vehicles. The government has pledged to invest £500 million between 2015 and 2020 into ULEVs. This is likely to boost demand for these vehicles, benefiting dealers. Grants for infrastructure will also be important, since more charging stations will be needed as more people drive electric cars.

What lies ahead

As discretionary spending is expected to suffer from widespread uncertainty over the next five years, financing deals and other methods of attracting consumers will need to be adjusted.

The market for used cars may expand at the expense of new car dealers due to weak consumer confidence and a reduction in financing deals. Future increases in interest rates are likely to increase the cost of finance deals.

Brexit Implications

The New Car and Light Motor Vehicle Dealers industry is heavily affected by trends in motor vehicle manufacturing and is therefore also affected by changes in the exchange rate. Imports of cars from Europe, Asia and the United States account for the majority of retail sales.

The value of the pound fell following the EU referendum, leading to an increase in purchase costs as car imports became more expensive. The prolonged depreciation is likely to lead to higher motor vehicle prices for UK consumers, which may reduce demand. However, operators are unlikely to fully pass on costs to consumers with consumer confidence currently constrained. Profit is expected to fall in the short term as economic uncertainty affects new car purchases.

However, Vehicle Excise Duty changes in 2017 caused new car registrations to increase by 6.2% in the first quarter of the year, according to the Society of Motor Manufacturers and Traders.

Increased operating costs are expected to slow sales later in the year as the weak pound affects fuel prices. This could also limit demand, as rising operating costs discourage driving and consumers may switch to public transport.

In the long term, the potential erection of trade barriers once the United Kingdom leaves the European Union could threaten the industry, as tariffs would limit margins and discourage demand for vehicles. The government aims to implement a temporary customs union to ease the process

*Source IBISWorld, New Car & Light Motor Vehicle Dealers in the UK/IPA Insight Centre*Automotive