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Hilco Smart Insights: Automotive Industry

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The Third Quarter is a Near Miss

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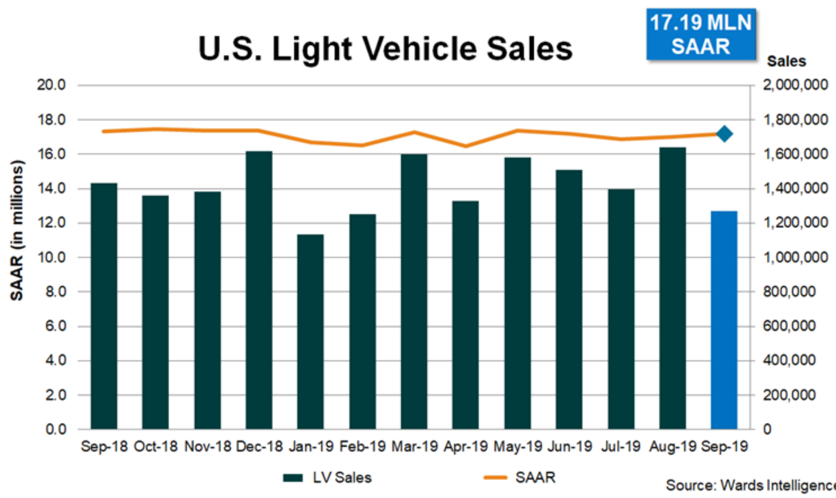

The sales differential between the third quarter of 2019 and the third quarter of 2018 was less than 2,000 vehicles. That is how close the third quarter came to being the first in two years to avoid a year-over-year decrease. In hindsight, I am sure there are OEMs that might have opted to sell a few more units to fleet customers. Total 2019 fleet sales were up 5.8% through September and now represent 17.4% of the overall market. Nonetheless, most industry insiders are happy with the result considering the threat from storms Dorian and Imelda, a drone attack on oil refineries in Saudi Arabia, a labor strike against GM, and ongoing trade disputes with most markets around the globe. Sales for the first nine months of the year are down only 1.6% from the prior year, and the seasonally adjusted annual rate (SAAR) is back over 17 million vehicles.

The UAW labor contracts at GM, Ford, and FCA (Chrysler) expired on September 14. As has been the practice in the past, the UAW identified a target company for negotiating purposes which it then used as the pattern for negotiating with the two remaining companies. Maintaining health care benefits and mitigating the use of temporary workers are important issues, but GM probably secured the target on its back last November when it confirmed that no new vehicle programs had been allocated to five of its U.S. manufacturing plants. As a consolation, GM was prepared to build batteries for electric vehicles at a yet-to-be-named UAW plant. However, having been given a glimpse into a future based on electrified vehicles, which appeared to herald an era of fewer workers and lower wages, the UAW rejected the offer. The supply chain for the auto industry is measured in days so it did not take long for the impact from the strike to spread. Many GM suppliers are making temporary layoffs and/or slowing production. With overall capacity utilization languishing near 70%, this is a battle that GM cannot afford to lose. On the other hand, at a daily cost of up to $100 million, is it a battle that GM can afford to win? The UAW is making Cobra payments on behalf of striking members in order to maintain their health care benefits, but how long can union members afford to live off the modest strike benefits of $250 a week? As the two sides enter their 4th week of negotiations, there seems little hope of a near-term resolution.

On October 1, the Institute for Supply Management reported its Factory Index had contracted for a second consecutive month. With a score of 47.8 in September, the lowest since June 2009, the result missed all estimates in a Bloomberg survey that had called for an increase from August's 49.1. Even before the disappointing economic data, the automotive industry was sensing the need to prepare for the worst. Dealers are concentrating on increasing their used-to-new sales ratio, cutting operating costs, increasing scale, and trimming their inventories. The OEMs are deferring non-essential capital expenditures and forming alliances to slash development and manufacturing costs of new technology.

Finance Cost	Fuel Cost	Inventory	Incentives
5.8% APR	$2.68 per gallon	68 days	$3,975 per vehicle
-10 bp MOM	+$0.07 MOM	+5 days MOM	+$11 MOM
-10 bp YOY	-$0.19 YOY	+3 days YOY	+$184 YOY

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