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Can the market defy gravity again in 2015? Not without a plan

By Professor Jim Saker

One of the strangest phenomena in the economy over the past two years has been the rise in sales in the retail automotive sector. With most of Europe in economic decline, or in the case of Germany and France plateauing, it is strange that car sales in Britain have not only continued to rise, but at an unprecedented rate. The burning question is whether this is going to continue in 2015?

Many analysts have tried to unpack the reasons for the continued rise. Some have suggested that PPI claims gave an impetus, while others have suggested that the state of the housing market has left people more disposable income to spend on cars. Some have argued that if you are in work and on a stable income then there is a level of consumer confidence that has allowed people to budget more effectively to accommodate a new car purchase.

In reality, the only factor that in any way corresponds to the rise in car sales is the rise in the number of PCPs being sold. The attitude to ownership and the cheap leasing arrangements have undoubtedly affected the momentum that has driven sales.

Apart from at the top end, most people buy cars because it makes economic sense for them to do so. Evidence shows that most of the growth has been in downsize to vehicles that are more fuel-efficient and incur lower vehicle tax. So a combination of easy payment schemes and lower running costs appear to account for the growth.

How will an election year affect the new car market?
The challenge is whether these factors will continue to drive market growth in 2015. The evidence would suggest that the market will remain strong into the new year. The uncertainty comes from factors both outside and within the sector.

One of the biggest barriers to business and customer confidence is uncertainty. With a general election looming, there is a risk that this may impact on sales, especially if the result is indecisive.

Perhaps the biggest challenge will, in fact, come from within the sector. The rise in the market and the fact that it is based on PCPs means there will potentially be a glut of three-year-old cars coming on to the market. This will inevitably put downward pressure on used car prices. If the rise in PCPs started in 2012, then the pressure should start to be felt in the fourth quarter of 2015 and into 2016. This could potentially have a major impact on dealer profitability.

One of the most interesting issues will be the handling of disaffected customers who return a car with a higher-than-agreed mileage or in a condition that does not meet the standard required. There has been little research done on the percentage number of walkaways in a mass market situation.

Most dealers are obviously trying to avoid this situation by attempting to get customers to trade up within the time period of the existing contract. Not only does this help to overcome the problem of customer dissatisfaction, but also spreads out the time when the lease cars are being returned.

Another problem beginning to emerge is in the low-end PCP returns of the luxury sector manufacturers. There is some evidence that advantageous lease arrangements have attracted customers from the mass market who are quite happy to pay the low payments, but end up trashing the car and then walking away from any further repurchase.

To what extent this will be a problem is yet to be fully analysed, but if it becomes more prevalent it may affect dealer profitability in the long run.

The PCP challenges in the year ahead
The challenge of used car prices falling with a glut of stock coming back to the dealership could impact negatively on cash flow and put pressure on dealerships that are not prepared for this financially.

For franchises that went into PCPs early in their life cycle, there will undoubtedly be a need for them to carefully plan their used car stock holding in the last quarter of 2015. Unless the balance between the new car PCP offering and the used car scheme is synchronised between the manufacturers and the dealers there could be major problems.

There is an old mantra that failing to plan is planning to fail. It is my belief looking at the evidence that planning in 2015 is going to be critical. Planning for PCP returns, handling potentially disaffected customers and trying to accommodate falling used car prices are going to be some of the major challenges in the new year. A strong retail market is great for business, but needs the same level of good management that was required when the sector took a hit during the financial crisis.

May yours be a well planned and prosperous new year.

“Planning for PCP returns, handling potentially disaffected customers and trying to accommodate falling used car prices are going to be some of the major challenges in the new year”

Professor Jim Saker is director of the Centre for Automotive Management at Loughborough University’s Business School and an AM Awards judge. He has been involved in the automotive industry for more than 20 years.