MOODY'S ANALYTICS

ANALYSIS
27 OCTOBER, 2020

Prepared by

Loc Quach
Loc.Quach@moodys.com
Economist

Contact Us

Email
help@economy.com

U.S./Canada
+1.866.275.3266

EMEA
+44.20.7772.5454 (London)
+420.224.222.929 (Prague)

Asia/Pacific
+852.3551.3077

All Others
+1.610.235.5299

Web
www.economy.com
www.moodysanalytics.com

Wholesale Used-Vehicle Price Report: 2020Q3

INTRODUCTION

U.S. wholesale used-vehicle retention value growth has been muted over the last two months after an unprecedented rise. Retention value rose 38% from April to July, as Americans prefer to drive instead of using public transportation to limit their exposure to COVID-19. This rise ended just as rapidly as it started. Since July, seasonally adjusted retention value has moved sideways. This dramatic turnaround is attributable to two factors: The resumption of vehicle manufacturing is providing consumers with the option to purchase a new vehicle instead of a used one, and job creation has decelerated so the labor market is not providing the used-vehicle demand support it did over the three months following April.

Wholesale Used-Vehicle Price Report: 2020Q3

BY LOC QUACH

U.S. wholesale used-vehicle retention value growth has been muted over the last two months after an unprecedented rise (see Chart 1). Retention value rose 38% from April to July, as Americans prefer to drive instead of using public transportation to limit their exposure to COVID-19. This rise ended just as rapidly as it started. Since July, seasonally adjusted retention value has moved sideways. This dramatic turnaround is attributable to two factors:

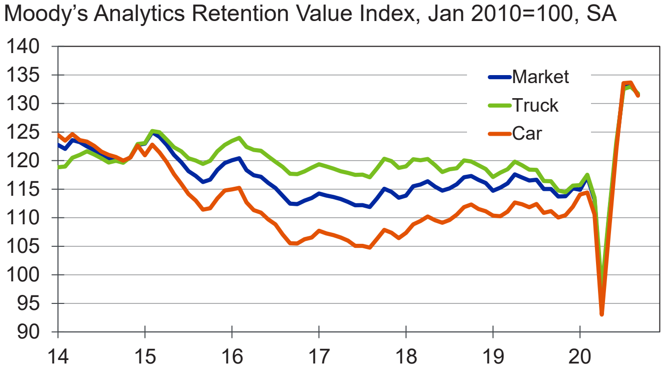
1. Resumption of vehicle manufacturing is providing consumers with the option to purchase a new vehicle instead of a used one.
2. Job creation has decelerated so the labor market is not providing the used-vehicle demand support it did over the three months following April.

New-vehicle supply revved up significantly after manufacturers brought their plants back to life, providing consumers with the option to purchase a new vehicle instead of a used one. Manufacturers rapidly shut down their factories when COVID-19 began to spread in earnest on U.S. soil to prevent the transmission of the disease among their workforce. Since then, automakers have brought back workers and devised ways to produce vehicles without spreading the disease. Since the April 2020 trough, U.S. vehicle manufacturing employment has bounced back rapidly, with industry employment making up most of the ground it lost in March and April (see Chart 2). With factories humming again, manufacturers are shipping cars to dealerships and some consumers have migrated from the used-vehicle lot to the new-vehicle options. Thanks to increased availability, new-vehicle sales have steadily marched up, rising from 9 million seasonally adjusted annualized units in April to 16.6 million units in September. The increased availability of new vehicles following the reopening of auto manufacturing in North America put a ceiling on used-vehicle retention value.

Job creation has slowed in recent months, removing a key area of support for used-vehicle demand (see Chart 3). After shedding jobs at an unprecedented rate in March and April, U.S. employment came roaring back. The labor market regained millions of jobs in subsequent months thanks in large part to fiscal and monetary stimulus. Job gains were concentrated in low-wage sectors, with 68% of the new jobs in lower-paying industries such as retail and leisure/hospitality. These are often

Chart 1: Retention Value Moves Sideways

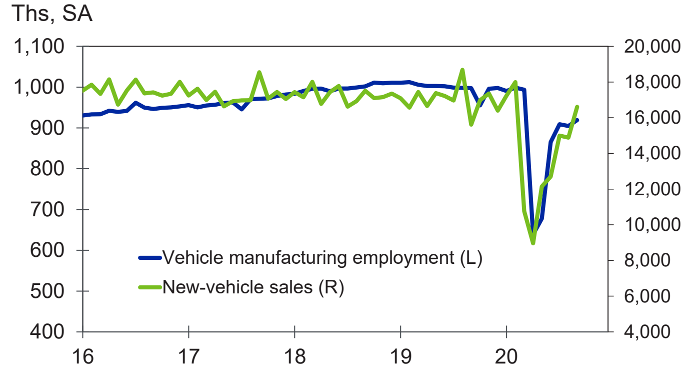
Moody's Analytics Retention Value Index, Jan 2010=100, SA



Sources: NADA, Moody's Analytics

Chart 2: New-Vehicle Supply Rebounds

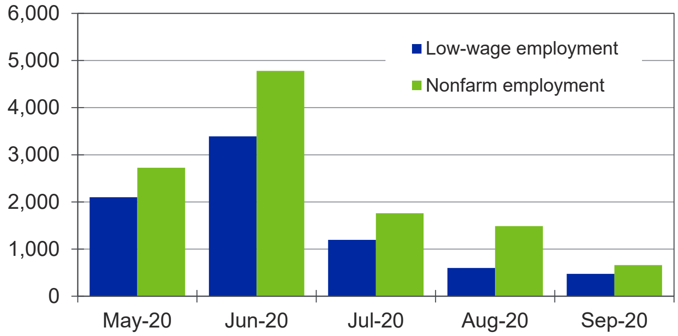
Ths, SA



Sources: U.S. Bureau of Labor Statistics, Autodata Corp., Moody's Analytics

Chart 3: Job Creation Slowing

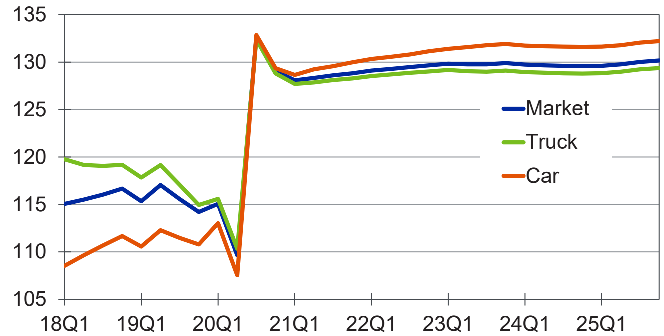
Ths, m/m difference, SA



Sources: U.S. Bureau of Labor Statistics, Moody's Analytics

Chart 4: Retention Value Forecast

Moody's Analytics Retention Value Index, Jan 2010=100, SA



Sources: NADA, Moody's Analytics

jobs where workers are not able to work from home and therefore need to commute. Given the possibility of COVID-19 exposure, the commute is preferably in a car. Because of the lower wages that many of these jobs offer, the newly employed or brought-back workers are more likely to purchase used vehicles instead of new ones. While the monetary authorities have committed to keeping interest rates low, the legislative branch has not been able to agree on the scale and scope of another stimulus bill. As a result, job creation has slowed; the 661,000 jobs gained in September is less than half the number gained in August. With job gains slowing down, there are fewer households who can create the space in their budget for a used vehicle.

The retention value of cars has risen more over the last few months than that of light trucks and SUVs. Strength in the retention value of passenger cars suggests consumers are purchasing vehicles to commute to work, rather than for social status or leisure reasons. The car retention value index has been lower than the truck/SUV retention value index for most of the last five years. However, car retention value has been rising faster over the last two years and rising demand for commuter vehicles during the pandemic has contributed to the process. Since bottoming out in April, the car retention value index has risen 41%, while the light-truck and SUV retention value index has risen 35%, erasing the gap between the two indexes. Cars are lower in price than their light-truck and SUV counterparts and are more fuel-efficient, making them the ideal vehicle type for commuting.

Vehicle retention value will decline modestly in the coming months. New-vehicle sales will gain ground and the labor market will provide less of a boost to used-vehicle demand. Retention values will inch upward beginning mid-2021 as a recovering labor market buoys demand (see Chart 4). Vehicle production will rise as automakers increasingly figure out how to manufacture vehicles while keeping the risk of infection down. Increased availability of new vehicles will eat into used-vehicle demand and ding retention value. Additionally, the robust job creation observed in the early part of the recovery is unlikely to be repeated. The recall of workers drove the initial surge of job gains, but the next stage of the job market recovery will depend on the fundamental strength of the economy. Job creation will pick up when a COVID-19 vaccine is developed and widely distributed. We expect this to happen around the middle of 2021.

A spike in COVID-19 cases is the main downside risk to the retention value forecast. A nationwide surge in new infections would lead businesses to rethink their reopening plans. Furthermore, state and local government officials in some areas of the country would require some nonessential businesses to close in COVID-19 hot spots. In such a scenario, the economy would fall into a double-dip recession. With the economy in recession again, consumer confidence would sink, and would-be vehicle purchasers would put away their wallets. The possibility of such a scenario is rising as the weather gets colder and people increasingly socialize indoors. After falling from July to mid-September, new cases are on the rise once again.

Congress not passing another stimulus bill is a secondary downside risk to the forecast. The baseline forecast assumes $1.5 trillion in additional fiscal stimulus in the first quarter of 2021. This stimulus includes aid to state and local governments, checks to households, and additional unemployment benefits. State and local governments' revenue streams have dried up amid the pandemic, leading to budget shortfalls. A lack of fiscal aid could result in state and local governments trimming their payrolls to balance their budgets. Furthermore, a lack of another stimulus check and expanded unemployment benefits would hit household budgets. Without additional fiscal stimulus, many households would think twice about committing to a large discretionary purchase like a vehicle.

Despite these risks and continued uncertainty, our baseline forecast is that retention values should remain well above 2020 levels throughout 2021. The fourth quarter will prove pivotal to making the rise in prices stick. During this period there will be results from not only the highly contested election, but also the Phase 3 trials for several vaccine candidates. The saying goes, "may you live in interesting times", and the next few months will certainly fit the bill.

About the Author

Loc Quach is an economist with the research group at Moody's Analytics. Loc forecasts used vehicle prices and contributes to automotive economics research. Loc previously covered the economies of Sweden, Israel, Hawaii, South Dakota, and more than a dozen U.S. metropolitan economies. He holds an MS in quantitative economics from California Lutheran University and a BA in economics from California State University, Long Beach.

About Moody's Analytics

Moody's Analytics provides financial intelligence and analytical tools supporting our clients' growth, efficiency and risk management objectives. The combination of our unparalleled expertise in risk, expansive information resources, and innovative application of technology helps today's business leaders confidently navigate an evolving marketplace. We are recognized for our industry-leading solutions, comprising research, data, software and professional services, assembled to deliver a seamless customer experience. Thousands of organizations worldwide have made us their trusted partner because of our uncompromising commitment to quality, client service, and integrity.

Concise and timely economic research by Moody's Analytics supports firms and policymakers in strategic planning, product and sales forecasting, credit risk and sensitivity management, and investment research. Our economic research publications provide in-depth analysis of the global economy, including the U.S. and all of its state and metropolitan areas, all European countries and their subnational areas, Asia, and the Americas. We track and forecast economic growth and cover specialized topics such as labor markets, housing, consumer spending and credit, output and income, mortgage activity, demographics, central bank behavior, and prices. We also provide real-time monitoring of macroeconomic indicators and analysis on timely topics such as monetary policy and sovereign risk. Our clients include multinational corporations, governments at all levels, central banks, financial regulators, retailers, mutual funds, financial institutions, utilities, residential and commercial real estate firms, insurance companies, and professional investors.

Moody's Analytics added the economic forecasting firm Economy.com to its portfolio in 2005. This unit is based in West Chester PA, a suburb of Philadelphia, with offices in London, Prague and Sydney. More information is available at www.economy.com.

Moody's Analytics is a subsidiary of Moody's Corporation (NYSE: MCO). Further information is available at www.moodysanalytics.com.

About Moody's Corporation

Moody's Analytics is a subsidiary of Moody's Corporation (NYSE: MCO). MCO reported revenue of $4.8 billion in 2019, employs more than 11,000 people worldwide and maintains a presence in more than 40 countries. Further information about Moody's Analytics is available at www.moodysanalytics.com.