COVID-19: impact on the automotive sector

In light of COVID-19's impact on the auto sector there are key actions they should consider.

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The COVID-19 outbreak has exposed several challenges for the automotive sector. Governments globally are preparing for a broader spread of the virus. South Korea, Italy and Japan are the most affected among the major industrialized economies. Consequently, 80 percent of automotive and related companies report that Coronavirus will have a direct impact on their 2020 revenues. 78 percent of companies do not have enough staff to run a full production line[1].

However, more than 80 percent of the world's auto supply chain is connected to China[2]. In January 2020 China's car sales plunged by 18 percent[3]. The China Passenger Car Association (CPCA) considers that the first two-month sales could decline by 40 percent or more compared to the same period in 2019. Production shortfalls resulting from supply chain disruptions in China will impact global automakers.

Hubei is one of the four major automobile production bases in China and has more than 100 automotive suppliers. Automotive plants in Hubei remained closed until March 11 and have now slowly started reopening. China is now over two months into the COVID-19 outbreak and vehicle sales have dropped to nearly zero. However, February, due to the Chinese New Year, has never been a strong month. March numbers will be much more representative of the real impact of the Coronavirus.

The situation in China is slowly getting better. According to the China Association of Automotive Manufacturers (CAAM), by the last week of February, more than 90 percent of over 300 automotive parts suppliers outside Hubei had resumed production. While all plants are open again, production rates were still low

[1] LMC Automotive Limited, Presentation: 20200312_Coronavirus Impact Assessment_for Amcham_vF.pdf, page 14, 1 und 3 Points.

[2] LMC Automotive Limited, Presentation: 20200312_Coronavirus Impact Assessment_for Amcham_vF.pdf, Page 16, 1 Point.

[3] LMC Automotive Limited, Presentation: 20200312_Coronavirus Impact Assessment_for Amcham_vF.pdf, Page 7, first comment).

given the dearth of orders from manufacturers and logistics problems. While Moody's Investor Service adjusted its global vehicle sales forecast to be down 2.5 percent in 2020 instead of a previous 0.9 percent drop due to the Covid-19 outbreak, it now looks in general more like a 6-8 percent down this year, with knock-on effects into 2021. However, people are not very happy to use public transport which makes the interest to buy cars seem huge. This is very much dependent on the restriction period required to contain the global spread of the COVID-19 pandemic and assumes there will be no subsequent second global wave. KPMG Automotive Institute believes in a global restart of the automotive sector in 3Q. The ongoing spread and different reaction to the Coronavirus in Europe will delay economic restart, despite ongoing, slow Chinese economic restart. Existing market vulnerabilities (e.g., trade tensions, declining sales) are likely to persist into Q3 given tight inventories (fewer than 6 weeks) and complex supply chains.

From our perspective it is most important to see COVID-19 as a global wave, which has to be simultaneously assessed from a global production and sales footprint. Companies with a heavy production and sales footprint in China already see a direct impact and will now start a recovery phase. Whereas companies with heavy production and sales footprint in mature Asia, Western Europa and North America will be affected when the wave arrives in these regions.

No one Top 10 OEM has the same production or sales footprint in the world. As the virus is evolving in waves around the world, the ones with heavy footprint in China, who had been hit very hard in February and March, will benefit from slow China economic recovery starting in April and will even see a small boom situation, as the local market will be supported by subsidies from local government.

Our prediction is that companies with either global balanced footprints or companies with heavy footprints in China will experience a lower impact than others, as China is slowly starting to recover already.

COVID-19's impact on the automotive sector may take an extended period of time to correct, but auto manufacturers can already consider the following actions:

- Protect and take care of employees: Follow the most conservative guidelines available among leading global and local health authorities (e.g., CDC, WHO). Support any impacted employees per health guidance.

- Create a contingency plan: model cash flows and debt levels, identify critical operations and employees. Create pragmatic, trigger-based contingency plans.

- Ensure a simple but well managed operating discipline, make sure that remote working is possible.

- Establish a team to focus on supply chain assessment and risk management. Conduct a value chain assessment of other risk factors that may escalate costs and impact service capabilities, take proactive action to address anticipated shortages. Develop supply chain support programs.

- Forecast global wave effects in production and sales and conduct scenario planning on how to redirect portions of supply to other sites based on sourcing strategies, potentially even rethink JIT models.

- Rethink the definition of safety and be aware that the protected customer does not only ask for virtual safety with cyber but also takes hygiene requirements (especially in car-sharing offerings) for granted.

- As personal travel has been reduced dramatically, think about changing modes of transportation, e.g., pre-booking air freight or rail capacity (potential switch of airplanes from passenger to cargo freight).

- Create a crisis response team to facilitate the open and consistent flow of accurate information between key stakeholders, maintaining stakeholder confidence and informing customers who will be impacted.

- Work with governments to explore potential tax benefits or to suspend tax payments.

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