Auto industry hit from Coronavirus could be even bigger than latest forecast

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Car production forecasts from the Society of Motor Manufacturers and Traders (SMMT) have suggested that UK auto output will fall by 200,000 to just below 1.1 million because of plant shutdowns caused by the Coronavirus; representing an 18% fall in output this year.

The forecast fall is based on the length of plant closures so far announced by the big assemblers, which have shut down given a collapse in demand, supply chain disruption, and to keep workers safe in line with the government mandating that all 'non essential' work should stop.

These existing shut downs will have a major impact on auto firms.

Jaguar Land Rover, for example, has stopped production for a month in the first instance, through to April 20th. Ignoring a planned Easter shutdown, JLR would have produced something in the range of 30,000 to 35,000 cars in that period.

Let's say that the value of those cars would be roughly £40,000 each (depending on the model mix and degree of options loaded onto cars). That gives a lost value of output in the range £1.2bn to £1.4bn just for JLR alone. While there would be some reduced costs in terms of components, there would still be a high degree of fixed costs.

And JLR – like other auto makers – may well be shut down for longer than a month. In that case the predicted decline of 200,000 units for the year could be a best (or least worst) case scenario.

Auto expert Professor Ian Henry of *AutoAnalysis* says that the output hit could be double the 200,000 hit in the event of extended shut downs.

There are other reasons as to why a -200,000 forecast may be the least bad scenario. For example, we don't know what will happen to demand for new cars when the crisis recedes; with unemployment spiking many in society will be facing a financial squeeze and could postpone spending on big ticket items like cars for some time.

And as I've noted before, as assemblers shut down, orders for component manufacturers dry up and there is a cascade effect on the supply chain. Supply chain firms have also shut down. While workers at Toyota are being paid wages for now, that will not be case in parts of the supply chain, which is why the government's labour retention scheme and other support for business is so critical in keeping capacity in place is so critical.

Without real support being made available quickly for firms, the fear is over a scarring effect on the long term capacity of UK automotive and manufacturing. The longer the shut downs go on, the more likely there will be a permanent impact on an industry that has already been struggling, and parts of an otherwise viable supply chain could be lost, in turn impacting on the ability of assemblers to restart production easily.

Such factors could see annual output falling below 1 million units which was the recent low point in UK auto output, back in the Global Financial Crisis of 2009.

All of which goes to show how difficult it is to do any sort of forecast for auto output and sales at the moment given uncertainty over the scale of the economic downturn caused by the Coronavirus crisis, its likely duration or what shape a recovery could come in.

What we can say is that this is the biggest shock that the sector has ever experienced. Sales in China were down by 80% in February – if that sort of downturn takes place in European markets over several months then we may see a drop in sales of the order of 20% for the year.

But how that impacts on production in part depends on what support is offered to auto firms later in the year. While scrappage schemes may not be appropriate right now – given the need to keep customers out of dealers' show rooms to stop the virus spreading – such measures may be needed later in the year.

From where we stand now, a fall in production of 200,000 units for the year may be a best case scenario. That's pretty disastrous for an industry that was already under considerable pressure given the shift away from diesels and Brexit uncertainty, and given the need to invest heavily in new technologies.

There also the issue of how the major carmakers will respond to the crisis, as they will face a big cash squeeze as consumers postpone purchasing cars. While auto firms' plants in China are just coming back into action, they are closed in Europe and the US. Ford for example has just suspended dividends and has drawn down some $15.4bn in credit lines.

The crisis comes at a time when International auto markets had anyway been slowing or stagnating, while at the same time car firms are having to invest huge amounts on a raft of new technologies, especially electric vehicles (EVs). A big squeeze is effectively playing out, and scale is seen as increasingly important for car firms.

So the shut downs will weaken firms and push them further to merge and consolidate. Auto firms will review investments and what models they produce, and where.

That poses further big questions over the position of some UK plants which anyway face uncertainty over the nature of the UK's trading relationship with Europe at the end of 2020.