Stop-start: Auto aftermarket sales have stalled because of COVID-19, but a demand surge is on the horizon

Sales of aftermarket automotive parts are taking a hit. Because of COVID-19, the economy has slipped into recession, and people are staying home, putting less wear and tear on their cars. The biggest factor in aftermarket parts demand-- is vehicle miles traveled (VMT)–which is likely to remain depressed as work-from-home and online shopping become permanent features of our economy. The good news is that demand may rebound sooner than expected, because the new cars purchased a few years ago–during a period of strong sales–will reach the prime age for replacement parts. The trick for parts suppliers will be to cut costs to reflect the current drop in demand, but also get ready for a pop in demand in a year or two.

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Automotive aftermarket parts companies face a dilemma: they need to adapt to a sudden and unexpected drop in demand, but also need to be ready for a demand surge in a year or two.

As the country endures the economic downturn brought about by the response to COVID-19, demand for replacement parts has declined. This decline has been made steeper by the quarantine measures imposed during the outbreak, since they have significantly curtailed people's need to drive: Fewer miles driven means fewer parts and repairs.

History suggests that recession-induced drops in vehicle miles traveled (VMT) tend to be long-lasting. VMT is usually slower to rebound than the overall economy. The current downturn is likely to result in an unusually large drop in VMT, as a result of a sharp drop in commuting and shopping trips because of COVID-19 stay-at-home measures.

So, are aftermarket sales doomed?

No, but the business faces several years of turmoil. While VMT may be depressed for a long time to come, the decline in the aftermarket parts business may prove to be relatively short-lived. That's because a significant percentage of vehicles purchased in the past few years will soon reach the "sweet spot" age for repairs, reigniting the demand for aftermarket parts and services.

Aftermarket companies will need to carry out a delicate balancing act: They must make cost-cutting measures to compensate for dwindling sales over the next couple of years, but refrain from cutting too deeply so they can take full advantage of the rebound once it arrives.

The aftermarket is lucrative, but not anti-cyclical

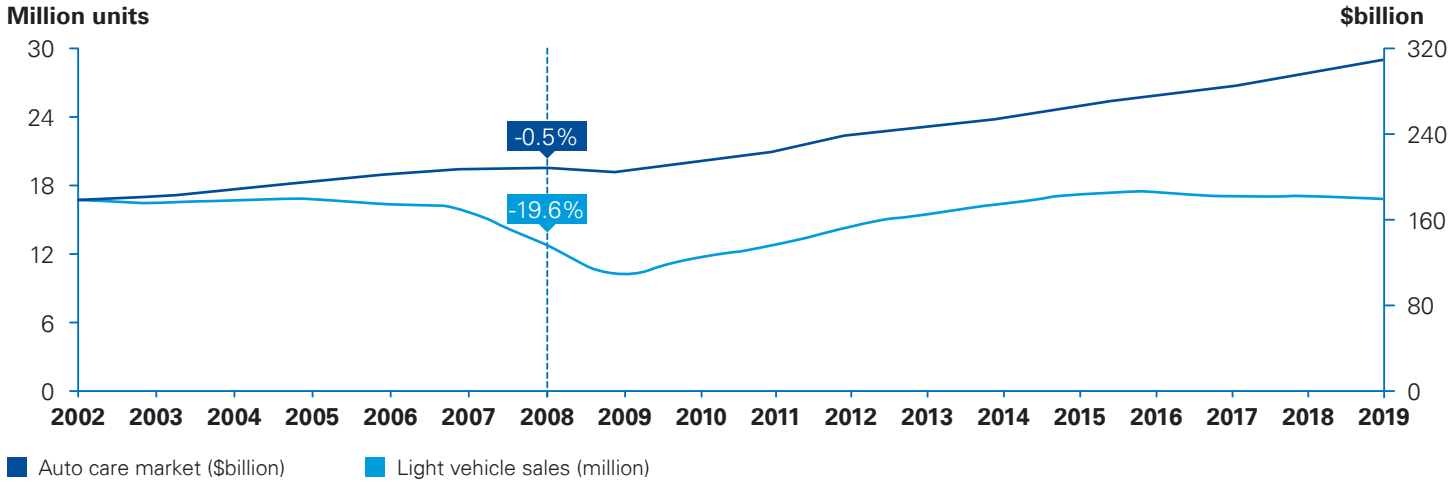
The automotive aftermarket—parts and services—encompasses product categories corresponding to all the systems in today's vehicles: drive train, cooling, exhaust, steering, suspension, and brakes to name a few. In 2019, U.S. aftermarket revenue was more than $210 billion.[1]

The aftermarket business is also highly profitable for automakers and Tier 1 parts suppliers, commanding far larger gross margins than new-vehicle sales. Indeed, we estimate that aftermarket parts account for more than 50 percent of many automakers' profits. That means aftermarket sales are also critical for keeping these automakers and their suppliers afloat during times of economic uncertainty when new car sales typically decline sharply.

Demand for aftermarket parts is generally assumed to be counter-cyclical to new car sales: when a recession hits, people stop buying new cars and spend more on aftermarket parts to keep their aging cars running. But in the 2008-09 recession, despite a 20 percent drop in U.S. new car sales (Exhibit 1), aftermarket parts sales did not rise. Instead aftermarket sales dropped by about 1 percent. During the COVID-19 quarantine in the spring of 2020, the aftermarket declined by over 5 percent as compared to the same period in 2019—despite a boom in DIY repairs by people staying at home.

Exhibit 1. New car sales dropped 20 percent in the last recession, but aftermarket sales held up

US light vehicle sales (million units)[1] and auto care industry ($billion)[2], 2002–2019



Note: [1]LMC Auto; [2]Auto Care Factbook 2021; aftermarket size includes DIFM and DIY sales of auto parts and services including tires, trim automotive aftermarket, specialty equipment products, and collision repair body parts

[1]AutoCare Factbook 2021; KPMG analysis

Fewer miles, fewer parts

Three major factors determine aftermarket sales

Seasonality: Aftermarket parts sales are seasonal, concentrated in spring and summer, when people prepare their cars for long vacation trips. For example, car owners are more likely to get a timing chain replaced during warmer weather.

VMT: The more miles on the odometer, the more the vehicle needs maintenance and repairs. We estimate that the average maintenance cost for a vehicle's first 25,000 miles is $1,400. That increases to $4,100 after 100,000 miles.

Car age: When the average age of all the cars being driven increases, the aftermarket industry benefits. For example, vehicles between 6 and 11 years old are a large market for do-it-for-me (DIFM) type repairs. Also, older vehicles will typically require large and expensive powertrain and suspension work.

Our research shows that VMT has the largest impact on year-over-year change in aftermarket sales. Between 2002 and 2018, aftermarket sales generally trended higher as VMT rose.

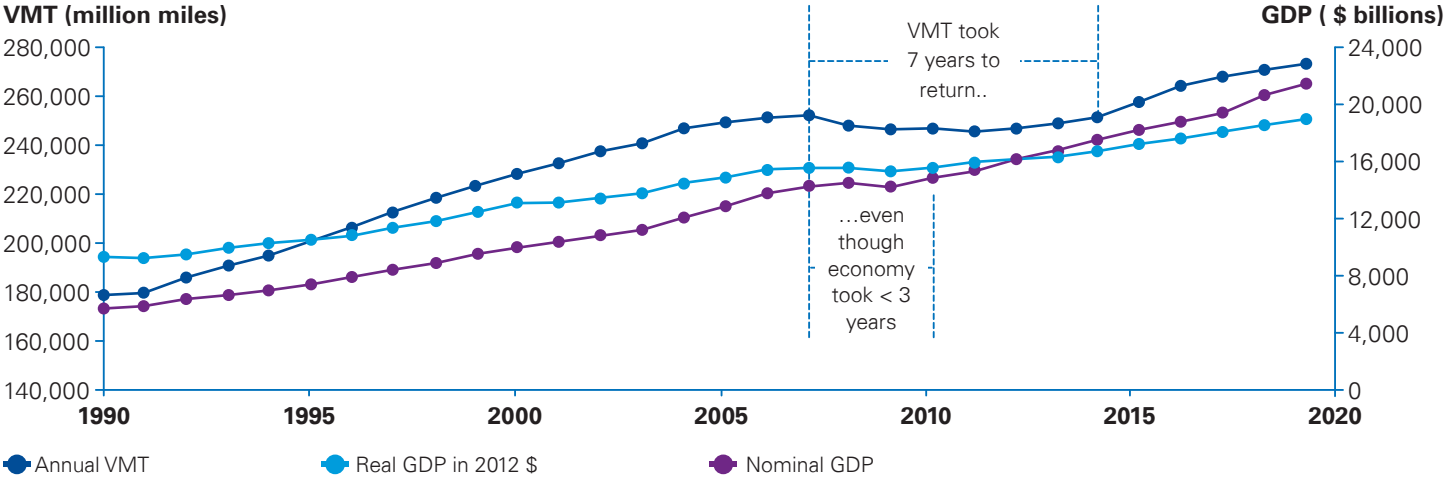
How COVID-19 reduced VMT—and could depress it for many years

Changes in VMT tend to be sticky—because they reflect changes in people's behavior. In the 2008 recession, while GDP rebounded in about three years, VMT took nearly seven years to return to previous levels (Exhibit 2). The current downturn is likely to be unprecedented in terms of changes to VMT. Because of the stay-at-home orders imposed following the COVID-19 outbreak, people drastically reduced their driving miles.

In April of 2020, VMT dropped by by more than 60 percent from April 2019.[2] Employees working from home no longer had to commute to offices. And with many stores closed, shopping trips were limited to only the most essential items. Recreational trips to bars, restaurants, and theaters also declined significantly (Exhibit 3).

Exhibit 2. In the last recession, GDP rebounded in 3 years, VMT took almost 7 years to recover

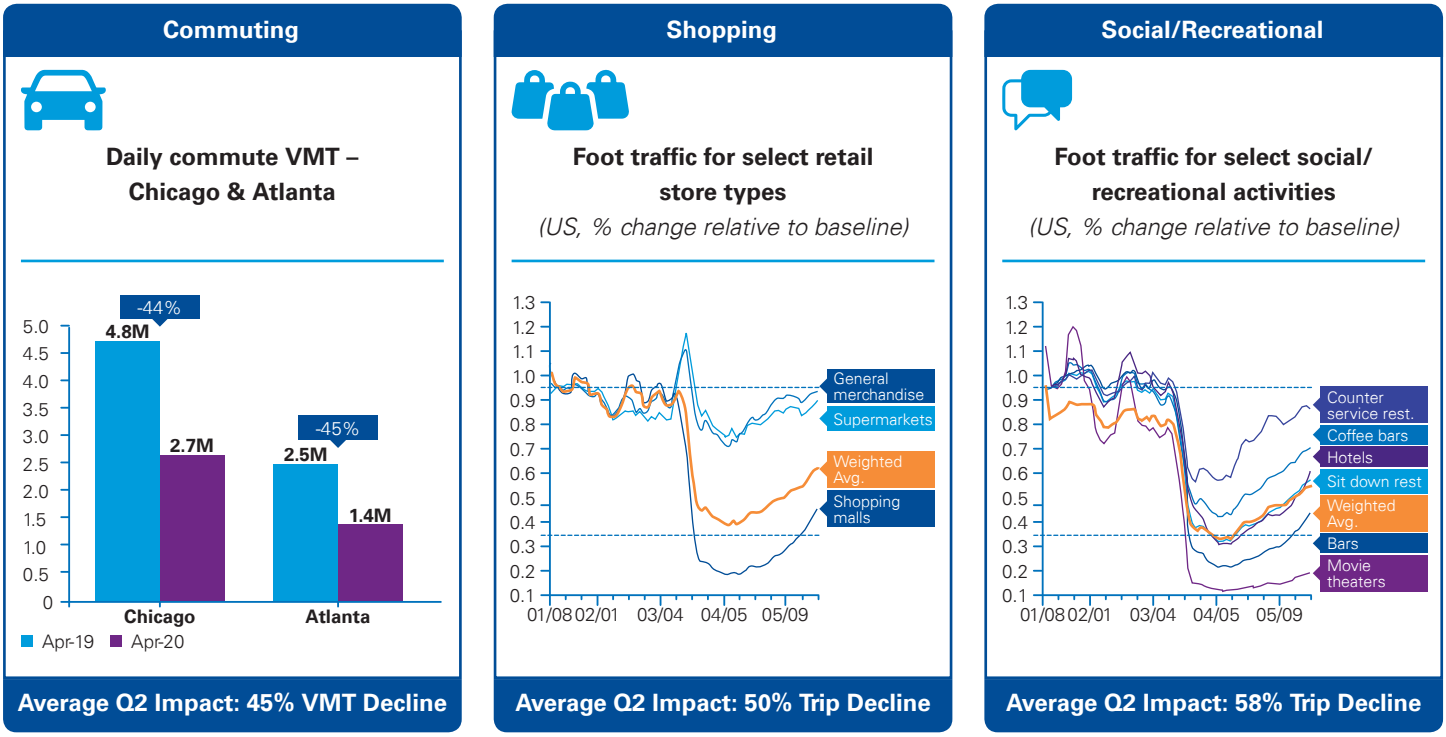
US Light Vehicle Miles Travelled (million miles), 1990-2020



Sources: US Federal Reserve

[2]KPMG analysis of Streetlight data

Exhibit 3. VMT has dropped across driving "missions"



Source: KPMG analysis of Streetlight data

Source: KPMG analysis of Safegraph data

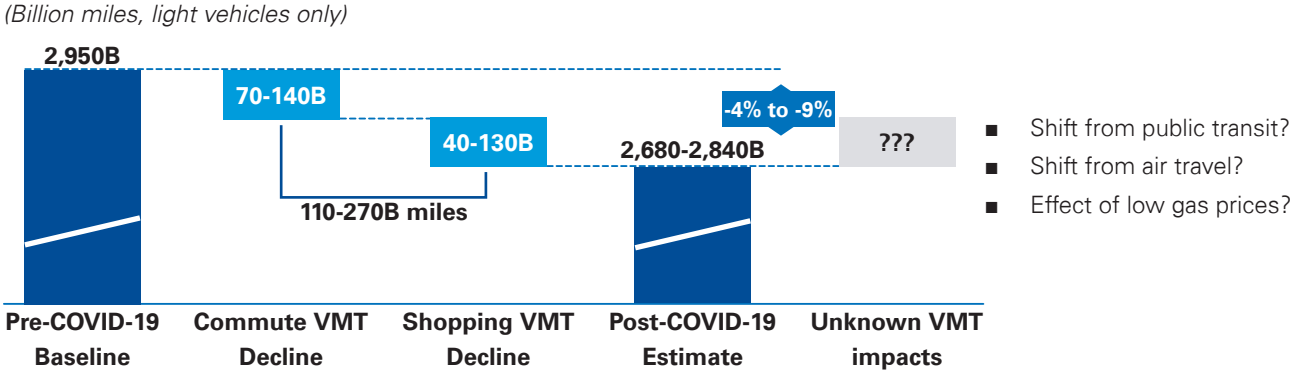
Source: KPMG analysis of Safegraph data

Given the decline in VMT, we estimate overall aftermarket revenue could decline around 13 percent this year from the 2019 level.

The question is, how long will this depressed level of VMT last this time?

Our research suggests that the behavioral changes occurring because of COVID will continue (for a detailed analysis, see Automotive's new reality: Fewer trips, fewer miles, fewer cars?[3] A Gartner survey of 300 CFOs suggests the trend toward remote working may continue, with companies planning to keep roughly 10 to 15 percent of their workforce as remote even after businesses reopen offices.[4] Likewise, a recent KPMG survey found that an average of 73 percent of respondents said they intended to continue using online shopping after stores reopen. That could reduce
VMT by as much as 9.2 percent, KPMG estimates (Exhibit 4).[5] Normally this would imply a permanent hit to demand for aftermarket parts.

Exhibit 4. Combined impact of VMT



[3]See Automotive's new reality: Fewer trips, fewer cars, fewer miles? KPMG, June 2020

[4]Gartner CFO Survey Reveals 74% Intend to Shift Some Employees to Remote Work Permanently, Gartner.com, April 3, 2020.

[5]Automotive's new reality: Fewer trips, fewer cars, fewer miles? KPMG, June 2020

A silver lining?

However, as noted, aftermarket sales are also strongly affected by vehicle age. Regardless of how much they are driven, cars need repairs and certain replacement parts—batteries, for example.

If they gauge demand by VMT alone, aftermarket suppliers risk paring back capacity for too long. There is a point where the rising average age of cars on the road starts to work in the aftermarket suppliers' favor, and the need for parts to repair aging vehicles will oflfset the loss in demand due to VMT.

Therefore, to arrive at a more accurate estimate of how aftermarket sales might be affected, we analyzed replacement part rates by the age of registered vehicles in the U.S. as well as VMT. New cars (three years old or less) log between 12,000 and 14,000 miles a year on average and generally need less maintenance.[6] Older cars typically need much more work, but owners are less inclined to spend money on non-essential repairs. And, as cars get older and more susceptible to breaking down, owners are tend to drive them less. They may use the car for short trips around town, but a longer excursion could create the risk of being stranded on the highway.

The good news for the aftermarket businss is that there was a slight boom in new-car sales between 2015 and 2019, which will expand the population of cars between three and seven years old by 2022. This is the age when repairs and maintenance requiring aftermarket parts start to occur. As a result, we estimate that aftermarket sales should begin to rebound in 2022 and recover to previous high levels by 2024 (Exhibit 5).

Auto parts suppliers need a strong strategy to benefit from online sales

With the COVID-19 stay-at-home orders and non-essential businesses closed, many consumers turned to e-commerce for their shopping needs.

That included automotive aftermarket parts: online sales of aftermarket parts increased by 47 percent during the COVID-19 lockdown.[7] Online browsing for auto parts for brands like NAPA and O'Reilly also increased during March.

This increase comes on top of an already growing trend toward aftermarket parts e-commerce.

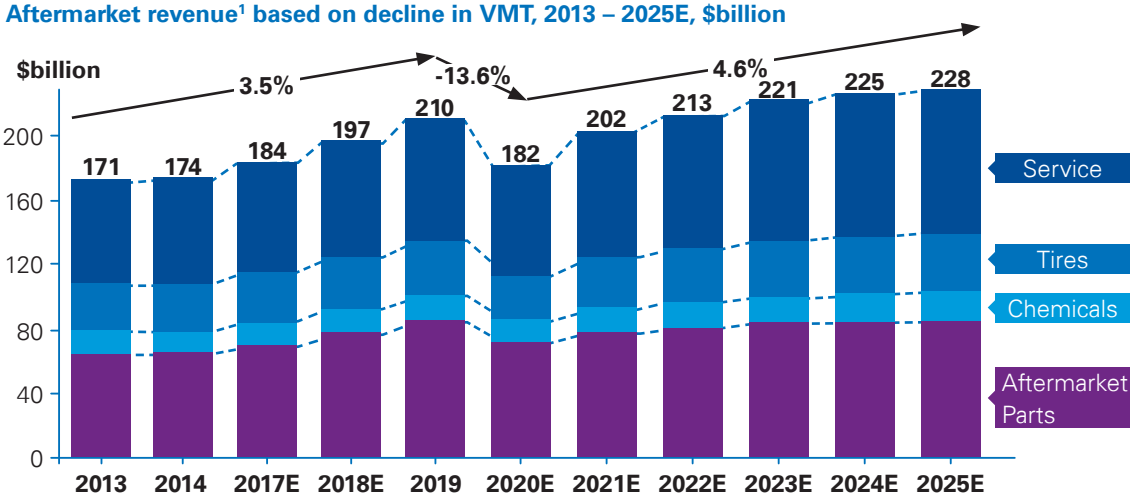
However, there are also challenges with online growth: e-commerce shoppers can easily compare prices, making the channel extremely price sensitive.

If auto parts manufacturers want to pursue online as a sales channel, they need to develop an e-commerce strategy, including channel-specific branding and pricing.

[6] 2017 NHTS Vehicle File
[7] Hedges & Company

Exhibit 5. Using our proprietary model, we project that demand for aftermarket parts and services could plummet in the next 1 to 2 years

Aftermarket revenue[1] based on decline in VMT, 2013 – 2025E, $billion



	CAGR 2013-19	CAGR 2019-20	CAGR 2020-25
Service	3.0%	-9.0%	5.4%
Tires	2.1%	-20.0%	6.0%
Chemicals	2.2%	-17.5%	4.7%
Aftermarket Parts	4.7%	-14.4%	3.3%

Note: [1]Market sizes for individual categories estimated based on replacement rates, car parc size and vintage; excludes collision parts and repair business, tools and equipment, and accessories sales
Sources: KPMG analysis; AutoCare Factbook 2021; Modern Tire Dealer

Action steps

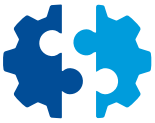
The decline in vehicle travel due to COVID-19 will have significant implications for aftermarket suppliers. Small companies, which rely heavily on aftermarket revenue, are likely to be impacted most. We believe that aftermarket parts manufacturers should be judicious in cutting costs to survive the current downturn but be prepared to ramp back up quickly when demand returns in 2022. This will require a careful rethink of capacity, product, channel, and pricing strategies.

Assess and review product portfolio

Suppliers need to assess their existing product portfolios and identify items that could be at risk over the next few years. VMT and age of car affect demand for various parts differently. For example, parts to repair accident damage and wear-and-tear replacement parts are almost entirely dependent on VMT, whereas batteries and rubber products have much more to do with age.

Adapt to changing channel mix

Companies need to tap emerging channels (such as online), while focusing on reducing costs and maintaining margins. E-commerce has blossomed during this downturn and online auto parts has been part of the boom. Online parts sales in May and June were up 45 percent over March levels.[8] While e-commerce is a growth engine, margins for this channel tends to be smaller.



Take advantage of M&A opportunities

Companies that can weather the storm over the next couple of years and make strategic acquisitions or investments are likely to do very well in the long term.

Manage cost and capacity through the cycle

Organizations should assess costs and find savings across the enterprise, including in operations, procurement, and SG&A. Footprint reductions may be necessary to maintain profitability, but must be balanced against the ability to meet demand when the demand rebounds.

[8] Coronavirus and Auto Aftermaket eCommerce News, hedgescompany.com

How KPMG can help

We see fundamental shifts in consumer behavior impacting Americans' need to drive, the distance they travel, and the mode of transportation they choose. This compels executives in the automotive industry to reconsider the historical approaches and assumptions underlying their demand forecasts and strategic plans. Our dedicated KPMG Automotive Strategy team can help executive successfully navigate the uncertain future by leveraging our long-standing history of insights and innovation and the power of data and analytics.

We assist clients with:

Targeted cost reduction and strategic growth initiatives—organic and inorganic

Considering implications of demand scenarios for current product portfolios

Analyzing a broader set of potential drivers of change and developing future scenarios

Determining the winning portfolio of products and services

Refining or rebuilding demand-forecast approach and framework

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