As the COVID-19 pandemic takes its toll, the automotive industry, a major contributor to the Gross Domestic Products of industrial markets, braces for a restart of its production facilities. But the process is a complex one with thousands of critical suppliers playing a role in the re-opening of North America’s economy.

Many automotive Original Equipment Manufacturers (OEMs) and their suppliers aspire to re-start production on May 4, 2020 and some will commence a phase-in process that could take up to three weeks after that. There is little doubt that production will start slow. A ‘catch-up’ of lost sales attributable to the lockdown period is unlikely. Estimated North American sales may see a drop of 25 percent to compensate for reduced consumer demand and production will follow suit. In 2019, North America produced 16.8 million vehicles and 17.4 million the year before. In 2020, North American production will likely struggle to surpass 14 million units given current market conditions.

The economic impact of the shut-down is being felt throughout the country. No one is immune. Coupled with dwindling demand, the OEMs are facing another problem. Used car prices have begun to experience a modest price decline over the last few months, but how the prices move going forward will have a noticeable impact on the performance of the various captive financing subsidiaries of the OEMs. Those subsidiaries are important catalysts to automotive sales as many consumers finance or lease automobiles to facilitate their purchase. As residual values fall, the financial service captives run the risk of losses when leases expire or on under-collateralized loans.

The movement in used car prices reinforces the impact of a lengthy shutdown of the economy. Persistent price deflation can have a debilitating impact on consumer confidence. Deflation was a major component of the Great Depression and reached -8.5 percent in Canada during 1932. Consumers and businesses deferred purchases and debt obligations became under-collateralized. Those conditions added fuel to an economy that already had 20 percent of the population unemployed, and Canadian industrial output fell to 58 percent from the late 1920s.

1 KPMG estimate, IHS
2 International Organization of Motor Vehicle Manufacturers
3 Canadian inflationcalculator.ca
4 Statistics Canada, The Canadian Economy in the Great Depression
Readers can appreciate the concern experienced by businesses everywhere and the hopeful optimism that OEMs have for a May 4 re-start date, even if it’s modest first steps. And suppliers will face challenges if they are not able to keep pace with OEMs, as alternate sources of supply will be available given excess manufacturing capacity in every region of the world. That problem can exaggerate local and regional unemployment.

A beacon for worker safety

The most important factor in our efforts to restore the economy to its former operating level is the ability to restore confidence in consumer spending and restoring employment to its previous levels. All of the economy’s employees are consumers. The two are not mutually exclusive.

Canada’s Automotive Parts Manufacturers Association (APMA) has done an excellent job in guiding Canada’s automotive factories on physical distancing and workplace safety in light of the COVID-19 pandemic as the industry prepares to go back to work. The Canadian automotive industry must set an example for how to restore manufacturing activity in a safe and effective manner for its workforce. It needs to be one of the beacons that helps set a standard for others to follow.

Producing them is only half the battle – you have to sell them too

Re-opening automotive production facilities is only part of the battle. OEMs cannot afford to build excess unsaleable inventory – the financial strain to their balance sheets will be damaging. As the pressure mounts, the retail dealer networks across North America will have to follow the OEMs and open their retail locations as factories commence production.

The chain reaction is not hard to picture. Cleaning and sanitary services for dealer locations, as well as licensing and registration agencies, insurance companies, and accessory providers will all have to coordinate their opening with automotive dealers.

As the economic power switch is turned on, the need for a coordinated reopening of the economy becomes crucially important. If we don’t get it right, we are going to continue to be in the dark for some time to come.