

The European automotive sector has stalled

In Q3 2018, automobile production fell in the leading European economies. The principal cause of this disruption was the introduction of the new WLTP (Worldwide harmonized Light vehicles Test Procedures) anti-pollution standards, applicable to all new vehicles since 1st September 2018. European car dealerships turned to various commercial strategies to compensate for the turbulence in the automobile market over the summer. Nevertheless, the European car industry - particularly in Germany - has been hit hard by the consequences of this new certification standard. In a context already rendered difficult by American protectionist measures, the future of the sector now depends partly on the capacity of manufacturers to adapt their production chains, all the more so since the stricter RDE (Real Driving Emissions) standard is set to come into force for all new vehicles as of 1st September 2019.

The new anti-pollution standards are the main cause of the recent downturn in the automotive industry

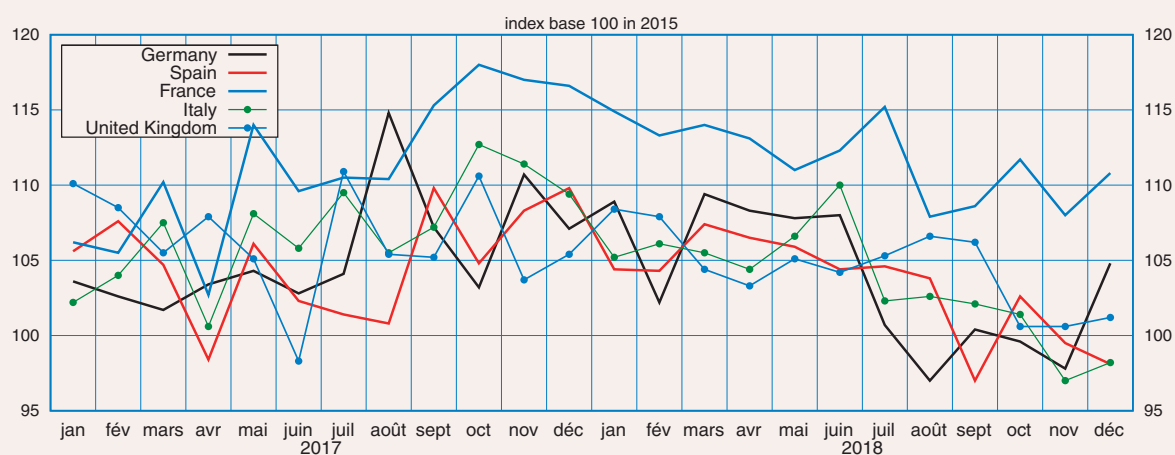
The Worldwide harmonized Light vehicles Test Procedures (WLTP) are a new set of certification standards measuring fuel consumption and emissions of CO₂ and other pollutants. This new standard has been adopted by the majority of the countries which make up the United Nations Economic Commission for Europe (i.e. the EU28, Norway, Iceland, Switzerland, Turkey and Israel), as well as Japan. It came into force in the European Union on 1st September 2017, applying exclusively to new models. As of 1st September 2018, it is now compulsory for all new vehicles. Since this date, models dating from before 1st September 2017 are only eligible for sale if they have already been road-registered or if the manufacturer has had them approved under the new standard.

In Q3 2018, the European automotive sector suffered as a result of the introduction of the WLTP standard. Automobile production accounts for 2.9% of the Eurozone's total output (Table). Production fell in all of the main Eurozone economies (*Graph 1*), and failed to bounce back in Q4. In Germany and Italy the slowdown began to show in July, with the industrial production index (IPI) for the automotive sector falling by 6.8% and 7.0% respectively against the preceding

month. The slowdown was felt slightly later in France (-5.5% in August) and Spain (-6.5% in September). In the United Kingdom, automobile production held up in Q3 but dipped in October (-6.7%). Overall, Germany was hit hardest: output from the automotive industry collapsed by 8% between Q2 and Q3 2018, the heaviest loss recorded since Q1 2009. Italy and Spain have also seen a decline in output (-4.3% and -3.4% respectively in Q3). However, this decline is a natural extension of recent trends observed in automobile production in these two countries, where the IPI in the automotive sector was already in difficulty in Q1 (-5.0% in Italy and -2.1% in Spain in Q1 2018).

In France, output held up reasonably well in Q3 2018 compared with its European neighbours, since the weak performance of August was offset by dynamic automobile output in July. The trend for the French automotive sector remains gloomy nonetheless, with decreases in all quarters in 2018. In the Eurozone, automobile output fell primarily as a result of a downturn in vehicle construction in July (-9.2%; *Graph 2*) and August (-5.5%). Bodywork construction also endured a poor spell in all of the major Eurozone economies in July (with decreases ranging from -2.4% in France to -8.4% in Germany). Nonetheless, output of automobile equipment remained broadly stable in 2018, though the weight of this segment was not sufficient to offset the decline in the output of vehicles and bodywork.

1- Industrial production indices in the automotive sector for the main European economies



Source: EUROSTAT

German industry has been hit hard

Among the European nations, the difficulties encountered by the automotive sector have been felt particularly strongly in Germany, where car-making has historically been one of the country's flagship industries. The automotive sector accounts for 20% of the total value added of the manufacturing industry, and 5% of total value added. German carmakers did not prepare sufficiently for the new standards. Volkswagen in particular, already penalised by the diesel emissions scandal, did not have time to adapt to the WLTP standards. By the summer of 2018 its production line was still not compliant with the new standards, and Volkswagen was accumulating a large number of models which had not passed the new tests.

Furthermore, WLTP requires all existing models of vehicles to obtain new certifications in their country of origin, according to their specific characteristics (engine type, gearbox, aerodynamic factors etc.). Ahead of the September deadline, Germany's certification agencies were overwhelmed by the volume of requests from the country's manufacturers. As a result, sales of Audi vehicles, one of the brands belonging to the Volkswagen group, collapsed by 69% in September. The Volkswagen group was forced to halt production at its Wolfsburg factory for several days, in order to limit their inventory of non-compliant vehicles. The group was also forced to stockpile vehicles which had already been manufactured but had not yet received certification, accumulating an

inventory of between 200,000 and 250,000 vehicles from the group's various brands, parked on the site of the future Berlin-Brandenburg airport.

In macroeconomic terms, German economic activity fell by 0.2% in Q3. Growth was penalised by manufacturing output and other sectors which depend on the automotive industry, such as retail and specialist activities. Mass storage of non-compliant vehicles probably accounts for the 0.7 points that inventory change contributed to growth in Q3 2018. Exports also fell sharply (-0.9%), hampered by weak automobile exports (-7.0% according to the seasonally-adjusted customs data; *Graph 3*), which account for around 13% of Germany's exports of goods and services.

Both investment and consumption have also been affected by the new standards

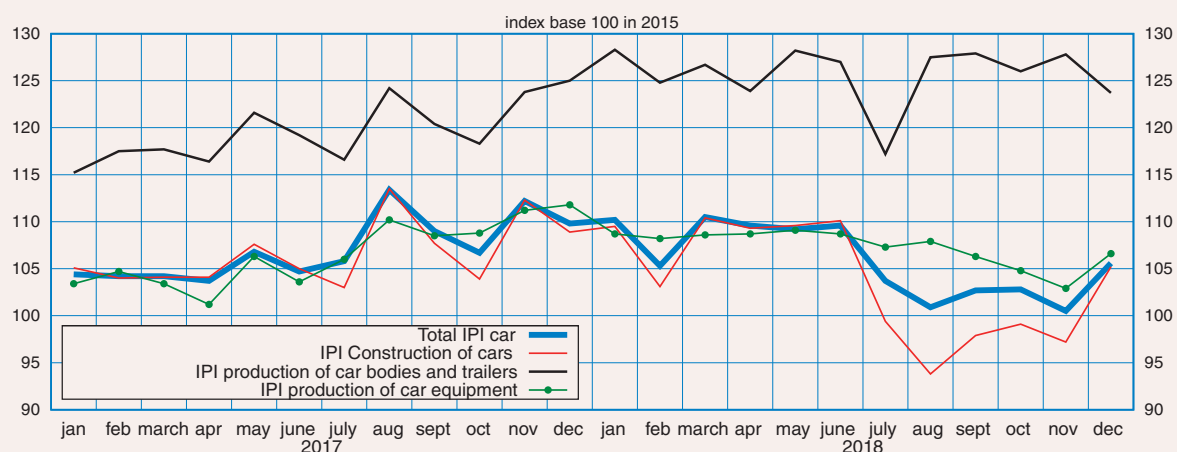
As a result of the new WLTP standards, registrations of new vehicles were also affected in summer 2018 (*Graph 4*). In August, the number of new vehicles road-registered in Europe was exceptional. The biggest increase was recorded in Spain (+35%), followed by France (+26%), the United Kingdom (+22%), then Italy and Germany (+18%). New registrations then dropped off in September, especially in Spain and Germany (-44% and -43%) but also in France (-37%) and to a lesser extent in the United Kingdom (-34%) and Italy (-32%). The peak in August and fall in September can be observed in the

Table - automotive industry as a proportion of total output (goods and services)

Germany	6,2 %
France	2,3 %
Italy	2,3 %
Spain	4,1 %
European union	2,7 %
Euro zone	2,9 %

Source: EUROSAT

2- Fluctuations in the components of the automobile industrial production index (IPI) in the Eurozone



Source: EUROSTAT

International developments

registration of both commercial vehicles (included in the calculations for corporate investment) and private vehicles (included in the calculations for household investment). Nonetheless, registrations of private vehicles were most affected. Depending on the country they account for between 80 and 90% of total vehicle registrations, and thus make the biggest contribution to monthly variations in total registration figures.

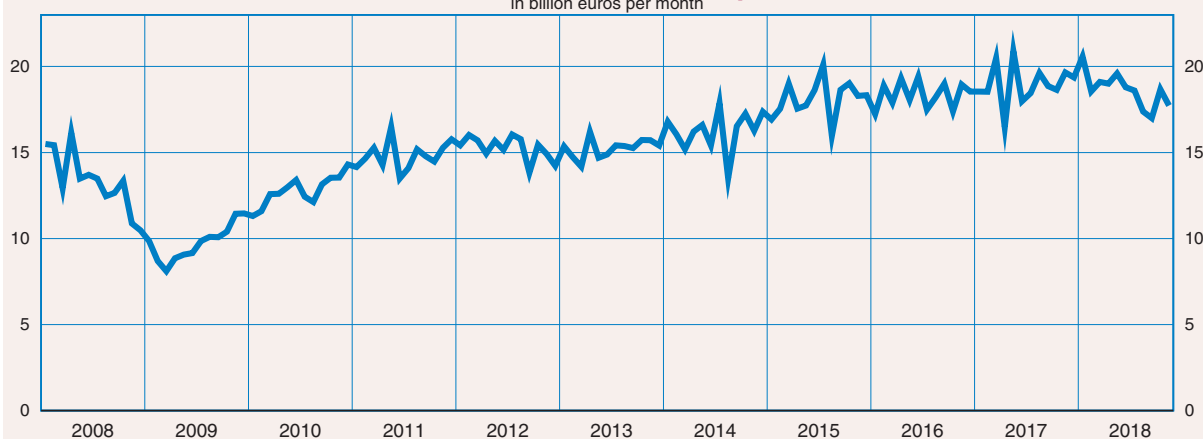
These substantial variations are partly a result of the commercial strategies adopted by dealerships in anticipation of the implementation of the WLTP standards. Since all vehicles registered after 1st September 2018 are required to meet the new standards, dealerships sought to reduce their vehicle inventories either by offering discounts in order to boost sales before the deadline, or else by registering the vehicles on their own account and selling them subsequently as "used cars with zero mileage."

The WLTP standards thus had an impact on the purchase price of new cars. In Spain in particular, prices slowed substantially in August, standing at +0.3% year-on-year (after +0.9% in July). Prices then recovered in September, at +1.1%. The effect was not quite so pronounced in all European countries. In Germany prices slowed less substantially in August, at +2.3% year-on-year (after +2.5% in July), then picked up pace again in September to stand at +3.0% by the end of the year.

The spike in sales induced by these discounts can be seen in the index for turnover from automobile sales. Spain recorded an exceptional month in August, with an increase of 6.0%. To a lesser extent, the turnover index for British car sales also increased in August: by 3.4%. In September, turnover in Spain and the United Kingdom fell by 8.9% and 7.7% respectively. This phenomenon was non-existent or negligible in other countries.

3 - German automobile exports

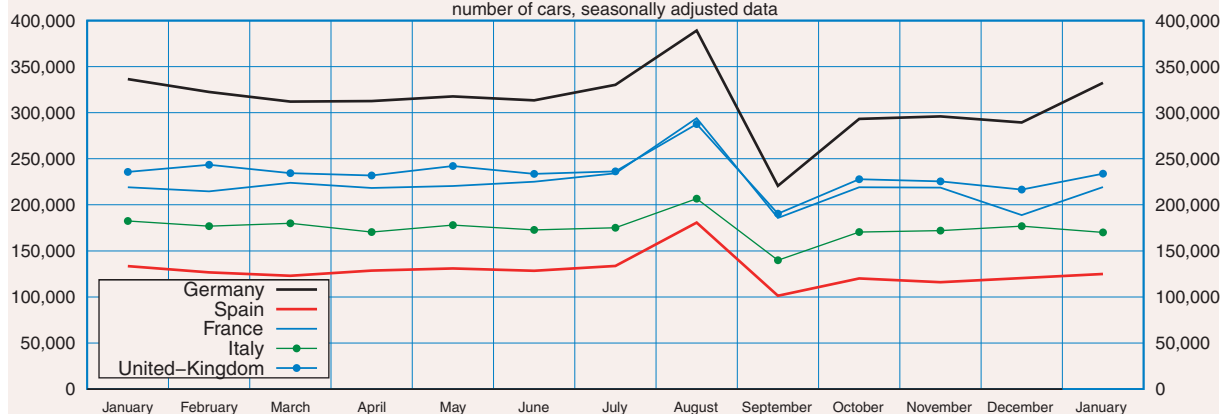
in billion euros per month



Source: German customs GENESIS, CVS treatment by INSEE

4 - Registrations of commercial and private vehicles in Europe in 2018

number of cars, seasonally adjusted data



Source: European automobile manufacturers' association (ACEA)

The relationship between the turnover index and the automobile price index allows us to assess the overall effects of this measure in real terms.

The turnover index, after deflation to account for automobile prices, peaked in those countries where significant discounts were on offer: in Spain and, to a lesser extent, in the United Kingdom (Graph 5). In countries which did not offer such generous discounts, dealerships seem to have instead opted for the advance registration strategy. They may thus have distorted the statistical measurements for household consumption and corporate investment, measurements which often make use of vehicle registration indicators.

How can the automotive sector get back on track?

Since October, the situation seems to be gradually improving in Germany. Volkswagen has confirmed that its fourteen best-selling models are now ready for the WLTP tests. Certain models, such as the Golf R, have had their power reduced in order to comply with the new standards. Others have been withdrawn from sale: under the new standards their emissions were too high, and would have cost too much in CO2 taxes.

In January 2019, the industrial production index for the automotive sector should pick up all over Europe. The situation should gradually return to normal in the first

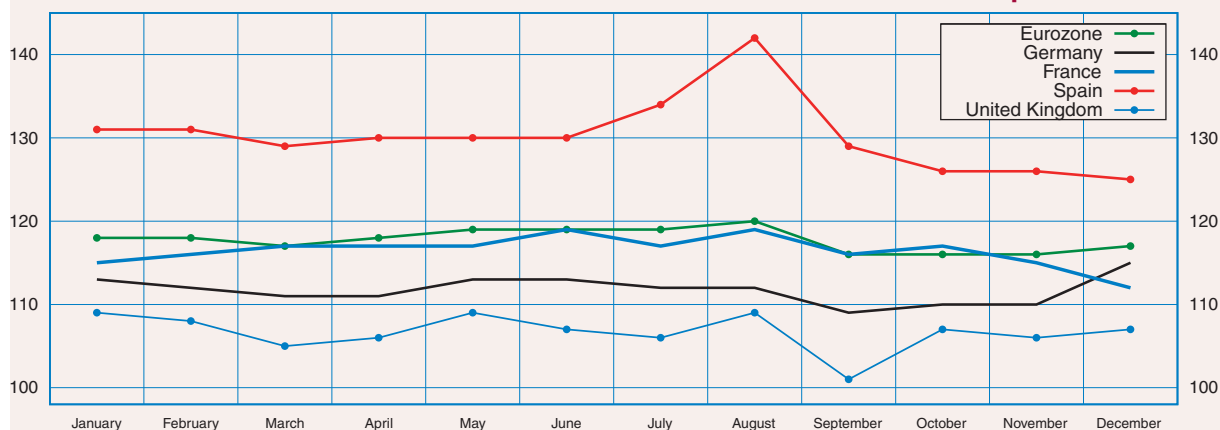
few months of the year, in keeping with the declarations of the managing director of Renault, who predicted that the company would be feeling the effects of the WLTP reform until April 2019. German car exports should also pick up again, allowing for a gradual reduction of the country's automobile inventory.

On the consumer side, purchasing intentions for vehicles remain stable; with purchasing power in reasonably good health in the Eurozone, this indicator would appear to suggest that automobile consumption will be dynamic over the coming months. Nonetheless, in December new vehicle registrations had not returned to their pre-summer level in Europe.

In addition to the new WLTP international standards, the European Union and a number of other countries have adopted a new procedure for measuring emissions in real road conditions, known as the RDE (Real Driving Emissions) system. This procedure came into force on 1st September 2017, exclusively for new models. However, on 1st September 2019 RDE testing will become mandatory for all new vehicles, which may lead to problems similar to those encountered in Q3 2018.

A number of other countries – including China, South Korea, Russia and India – have also signed up to the international WLTP standards, but have not yet published their implementation schedules. The effects of the WLTP standards have therefore not yet been felt outside Europe. ■

5- Variation in real terms of the turnover index for automobile sales in Europe in 2018



Source: EUROSTAT, Calculs INSEE