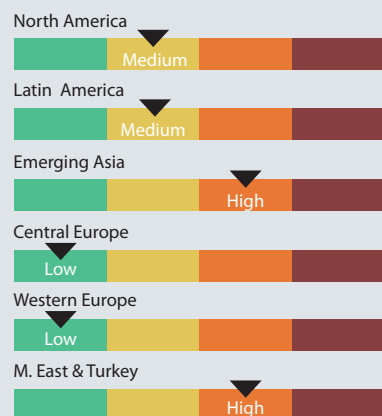




AUTOMOTIVE

COFACE REGIONAL SECTOR RISK ASSESSMENT



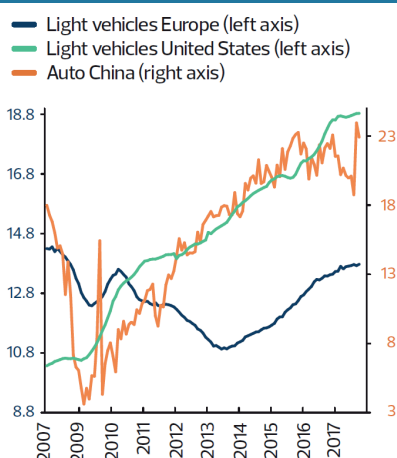
+ STRENGTHS

- Unprecedented period of innovation in the sector
- Recovery in demand in Europe
- Car manufacturers are among the largest investors in R&D worldwide

- WEAKNESSES

- Slowdown in China and the United States
- Situation in China with overcapacity and the ongoing rebalancing of its economy
- Increasingly restrictive anti-pollution standards requiring heavy investments
- Deteriorated credit risk in the United States and United Kingdom

SALES OF NEW VEHICLES, (YEAR-ON-YEAR)



Source: ACEA, Autodata, NBS

RISK ASSESSMENT

The global car market is heterogeneous, with the contrasts between the dynamic European markets and the constantly slowing US market. There is also the Chinese market which differs again as it is widely subsidised by the State.

The growth in car sales is slowing in China. The reasons behind this include notably the impact of the reduction in taxation on engines smaller than 1.6 litres, which enabled an upturn in the market. Competition between carmakers is also more intense, which has benefited the domestic ones, as well as the German groups thanks to their solid local presence.

In the United States, vehicle sales continue to slow. The light trucks segment which is holding up, allows the manufacturers to continue selling their production. There is a fall in the residual values of leased vehicles, which could have negative repercussions combined with the worsening credit risk.

In Western Europe, all the leading markets have been experiencing annual growth, with the exception of the United Kingdom, where the "success-story" could be facing challenges, mainly linked with the uncertainties.

DEMAND

Demand around the world varies, with a slowdown in the United States and more positive outlooks in China and Europe.

In China, doubts are growing concerning sales expansion. The tax reduction on small engine is not expected to last into 2018. We are therefore expecting a slowdown or a fall in sales. Finally, electric and hybrid vehicles are likely to continue to benefit from the enthusiasm for these being shown by Chinese consumers. The government is promoting these vehicles with the aim of limiting the levels of pollution endemic across China, as well as creating national champions. This promotion even takes the form of quantitative objectives to be achieved: in 2019, between 4% and 5% of each maker sales carmaker will consist of electric or hybrid vehicles. This plan has however been received with only lukewarm enthusiasm by the leading players in the sector who highlight the difficulty on implementing it.

In the United States, the raising of interest rates in June 2017 pushed up the cost of borrowing: the rate has risen from 4.9% in December 2016 to 5.6% at the end of June 2017. The credit quality (90% of new vehicles are financed this way) is declining in part because the maturities are reaching up to seven years (84 months), taking these borrowers out of the market, and exacerbating the loss of residual value of the vehicles. In addition, despite the historically low level of unemployment, the rate of participation in the labour market at the end of October 2017 was 4 percentage points below that of January 2007. Median wages however were up 3.1% between 2016 and 2017.

According to Eurostat, the eurozone's unemployment rate was 8.8% at the end of October 2017, a decrease of 1 percentage point compared with October 2016. Whilst it is still at high levels in Southern Europe, vehicle registrations remain dynamic there, driven by car hire operators and companies renewing their fleets, to take advantage of models with lower maintenance costs. In 2017, interest rates are expected to remain low and thus encourage vehicle credit as well as more recent financing schemes such as lease purchase (LP). However, demand is not likely to remain as strong as seen up to now, even though confidence levels in European households are expected to continue positive.

SUPPLY

Sales in Western Europe would seem to be heading towards a peak, whilst the Chinese market is expected to experience a number of wobbles.

Coface expects an increase in vehicle sales in mainland China of between 4% and 5% in 2018. The country is becoming a key player in terms of the production and sales of electric and/or hybrid vehicles. The central government is in effect strongly encouraging these technologies through tax rebates. Thus explaining the announcement by the Volkswagen group of the introduction of 25 new electric models in the country between 2020 and 2025, and its plans to invest USD 12 billion through its joint-ventures. The country is well prepared to hold on to its pole position in this field, via a committed policy of mobility, as well as through the acquisition of lithium producers in Latin America and in Australia.

In the United States, sales of new vehicles are likely to continue contracting in 2018. With the arrival of millions of ex-leased vehicles on the used car market, residual values are expected to fall 3% in 2018, according to the LMC Automotive economic intelligence consultancy, compared with 6% in 2017. On top of this there is increasing competition between carmakers, which is likely to shrink margins. Finally, the details of the NAFTA are the subject of intense renegotiations between Canada, the United States and Mexico. The proposals from the United States concerning the determination of the proportion of local production in each vehicle presents problems for the other two countries. It is calling for a higher level of equipment produced in the United States to be included, to the detriment of its partners.

Registrations in Western Europe are likely to increase in 2018. According to our calculations, the total sales of the leading carmakers and equipment manufacturers increased by almost 8% in the third quarter of 2017 year-on-year. However, the exiting by the United Kingdom from the EU, scheduled for March 2019, is likely to not only present risks for the UK car industry, but also lead to adjustments in the organisation of European production. Nevertheless, European carmakers and equipment manufacturers are at the forefront in the fields of driving assistance, as well as the reduction of particle emissions, thanks to the impetus given by public policy. In this latter field, the existence of a dense dealer network is likely to also help the European carmakers in resisting competition from the US carmaker Tesla.