Blog

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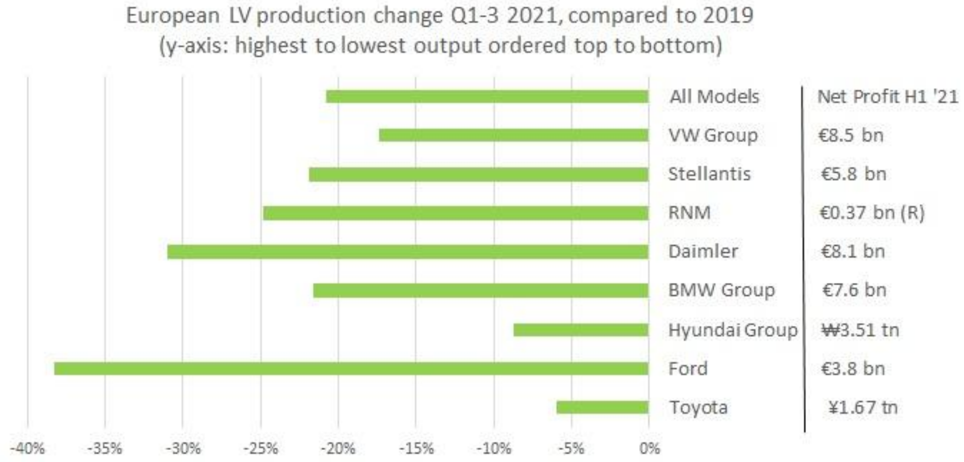
The impact of the procurement crisis on European OEMs

Early optimism by European automakers and analysts alike, with claims that vehicle output would improve markedly in the second half of 2021, has long since faded as the procurement crisis persists. The most recent setback has been the forced closure of semiconductor facilities in Malaysia to contain the latest COVID-19 outbreak. The crisis hinges upon raw material price increases, semiconductor shortages and bottlenecks in the production of intermediate products. Undeniably, the major constraint to European Light Vehicle output so far this year has been the scarcity of chips, which is estimated to account for roughly 80% of the total loss in output from our pre-crisis expectations. Meanwhile, shortages of other vehicle components, such as wiring harnesses and brake parts, have further exacerbated the slowdown, albeit to a lesser extent.

Through to the end of Q3 this year, we estimate that almost 1.5 million fewer vehicles were produced in Europe as a result of chip supply disruptions. These losses are substantial, so much so that vehicle inventories are running too low to adequately supply buoyant demand for new cars. The inverse is usually true, with demand dictating the level of supply. Despite this, and perhaps counterintuitively, OEMs have managed to improve profitability over the first half of 2021 (see chart below for H1 CY net profit figures) by prioritising high-margin models and raising vehicle prices to offset higher input costs. In essence, the procurement crisis has increasingly steered market power away from consumers. In addition, manufacturers have continued the cost-reduction work started before the pandemic, including both capacity and model line-up rationalisation.

Nonetheless, the situation remains suboptimal, with potential sales forgone as higher vehicle prices force some buyers out of the new car market. This is evidenced by the dramatic increase in second-hand car prices. Moreover, it is arguably no coincidence that Hyundai's and Toyota's management of the crisis, despite recently announced disruptions, has helped to support their respective global output levels (see chart below) and leave them well placed to gain market share and post healthy profits. The clear implication of this is that, if it were possible, manufacturers would supply more vehicles, thus reverting to a perfectly competitive market and lowering the price of new cars for consumers.



Source: LMC Automotive European Light Vehicle Production Forecast Note: (R) = Renault.

Unfortunately, supply constraints and inflationary pressures will almost certainly persist until the chip shortage is resolved, which will require greater chip allocation to the automotive industry. The cost and complex nature of semiconductor manufacturing means that it takes years for production capacity to expand. We therefore expect disruptions to European Light Vehicle production to continue until at least 2023, at which point output volumes are set to just about recover to 2019 (pre-pandemic) levels.