Bank of Ireland Sectors Team Motor H1 2021 Insights / Outlook H2 2021

July 2021

Bank of Ireland

Classification: Green

Pre-COVID Environment

The new car market peaked in 2016 at 146,600 units following strong growth from a low base. Demand for new cars went into decline from 2017 as the industry felt the impact of Brexit. By the end of 2019, new car sales fell c. 20% to 117,100 units from peak sales in 2016. Due to a weakened sterling, used passenger car imports from the UK market surged in the same period. Used imported cars reached record levels in 2019 at c. 114,000 units. New car demand in Ireland was dampened as used car values were impacted by cheaper imports from the UK. During the same period, consumer confusion began to rise concerning which engine type to choose in their next new car. This follows considerable media coverage on the future of the internal combustion engine and growth of electric vehicle (EV) sales.

Resilient Sector

FY 2020: Overall, new passenger car sales declined c. 25%, light commercial vehicle sales declined by c. 14% and used import sales declined by c. 30%. These full year headline figures hide the underlying trend in the recovery of vehicle sales last year. In the 32 week period from restarting the economy to year end, new vehicle registrations increased by c. 5%[1] due to strong levels of consumer demand. *[1]Excluding hire drive (HD) sales. Note HD sales declined c. 85% in 2020 due to the impact of COVID on tourism.*

H1 2021: Level 5 COVID restrictions were in place for the first 4.5 months of 2021 and the sector continues to show its resilience during the health crisis. Motor dealers continued to open for vehicle aftersales and consumers could visit dealers to have maintenance carried out. For new and used vehicle sales, dealers engaged with customers using digital methods such as personalised video messages and operated a "click and deliver" service. Dealers fully reopened for both sales and aftersales on 17th May. This was timely for dealers to order build ahead of the second sales peak commencing in July 2021.

Compared to pre-pandemic levels, this year new passenger car sales are running at c. 80% of 2019 levels. New van sales are c. 11% ahead of 2019 levels, highlighting increased demand for home deliveries. When hire drive sales are excluded, new passenger car sales are running at c. 90% of 2019 levels thus highlighting strong underlying retail demand. Used passenger car imports are c. 33% lower than in 2019 due to the impact of Brexit and changes to the treatment of vehicle registration tax for used imports in January of this year.

Brexit Impact

There are no tariffs for new vehicles retailed by motor franchises in Ireland as a result of Brexit. The impact is likely to reduce the inflow of privately imported used vehicles (currency dependent) due to the imposition of VAT and tariffs (for vehicles not manufactured in the UK). There are some exceptions to these new rules, however, increased costs and complexity are likely to deter private individuals importing used vehicles from the UK.

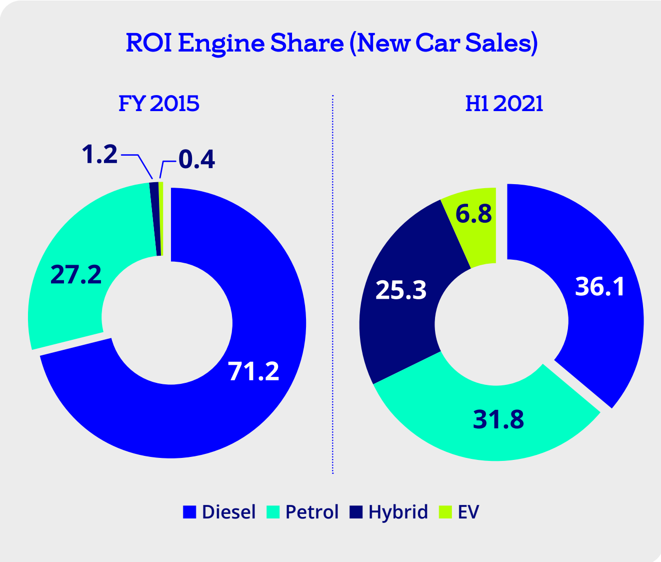
Motor dealers continue to import used vehicles from the UK where value is present. Dealers are commenting that higher costs now associated with importation of used cars from the UK are being passed on to consumers as used vehicle residual values are starting to recover here (due to lower volumes of used imports and higher consumer demand). This commentary is corroborated in recent editorials by 'Motor Trade Publishers' regarding used car values.

Vehicle parts distribution and supply was impacted earlier this year with longer lead times, particularly for parts that are distributed directly from the UK to ROI (distribution logistics varies by manufacturer). Motor franchises and dealers had predicted this delay and increased fast-moving parts inventories in Q4 2020. The sector has since reported improvements to parts supply.

Accelerating EV Sales

Looking back to 2015, the combined share of electric vehicles and hybrids was less than 2% of new car sales in Ireland. By 2020, this share had increased to almost 20%. The take up of these engines has further accelerated in H1 2021 with the combined share of EV's and hybrids now representing c. 32% of new car sales. Although the share of diesel cars has fallen each year since 2015, demand in Ireland remains strong at c. 36% when compared to the UK at c.10% and the EU at c. 23% (Q1 2021).

	H1 2021	H1 2020	H1 '21 v. H1 '20	**H1 2019**	**H1 '21 v. H1 '19**
New Cars[2]	**63,867**	52,885	+20.8%	**80,758**	**-20.9%**
New Vans	**17,027**	10,569	+61.1%	**15,317**	**+11.2%**
Combined Sales	**80,894**	63,454	+27.5%	**96,075**	**-15.8%**
[2]thereof, Hire Drive	***3,637***	*2,759*	*+31.8%*	***14,412***	***-74.8%***
Used Imports	**35,754**	22,787	+56.9%	**53,126**	**-32.7%**



Sales of electrically chargeable vehicles (ECV = BEV[3] + PHEV[4]) also ticked up across the EU this year as demonstrated in the table below. Attractive consumer incentives offered by countries such as France and Germany, coupled with greater choice of vehicles and increased consumer demand have further accelerated the demand for electric vehicles across Europe. At the end of the first quarter, Ireland ranked 6th in the EU for BEV take up (based on BEV percentage share of engine sales). By the end of H1 2021, the share of BEV sales in Ireland has further increased to almost 7% of new car sales.

	FY 2020		Q1 2021	
Engine Type	**EU**	**ROI**	**EU**	**ROI**
[3]BEV (battery only)	**5.4%**	**4.5%**	**5.7%**	**5.9%**
[4]PHEV (plug-in chargeable hybrid)	**5.1%**	**2.8%**	**8.1%**	**5.7%**
Total ECV (total electrically chargeable)	**10.5%**	**7.3%**	**13.8%**	**11.6%**

Manufacturers are investing heavily in battery production with several new production facilities now in operation in Europe. One example is Northvolt, a battery production company established by former Tesla executives in 2016 and based in Sweden. Northvolt is partnered with VW Group, BMW and Volvo and are targeting a 25% market share in Europe by 2030. To put the scale in perspective, the company announced a $14bn order from VW earlier this year. They also raised additional funding of $2.75bn in June this year to expand existing capacity. Others competing with Asian markets and based in Europe include Britishvolt and the Tesla gigafactory in Germany.

Volvo and Ford have announced intentions to cease production of their internal combustion engines for Europe by 2030 and Volkswagen Group by 2035. Others will follow with announcements in due course. Bloomberg New Energy Finance expect price parity between EVs and internal combustion vehicles by the middle of this decade. As a greater number of BEV's are produced, in terms of volume and choice of models for consumers, production costs will fall. Generally, the sector expects that BEV prices will be more in line with internal combustion vehicles toward the end of this decade. In the interim, government supports are vital to support the continued growth of electric vehicles in Ireland.

Declining Emissions

Car manufacturers must meet a new C02 emission target of 95g/km per vehicle sold this year. This new 2021 target becomes the revised baseline for proposed further reductions forming part of the European Green Deal. Emission targets for newly registered cars must reduce 15% by 2025 and reduce 37.5% by 2030 (from 2021 levels). The 2030 target is now under review by the European Commission (EC). Among proposals under discussion in the EC are a 55% emissions cut by 2030 followed by a ban on combustion engine sales by 2035. In order to achieve these targets, manufacturers will accelerate investment in battery production and increased choice of electric vehicles.

In 2019, C02 emissions from new passenger cars sold in Ireland was c. 114g/km (compare EU at c.122g/km). In 2020, C02 emissions here fell 7% to c. 106g/km. In the first half of 2021, C02 emissions from new car sales have further declined in Ireland to 97.1g/km. This is due to the increased uptake of electric and hybrid vehicles coupled with lower emissions from the latest petrol and diesel engines sold.

The Irish government made extensive changes to vehicle registration tax effective from 1st January 2021, which had the net effect of increasing prices for new low emission cars. Increasing taxation on new vehicles will impact the speed of recovery to pre-Brexit levels of sales, thus taking longer to remove older and higher polluting cars from circulation. I can think of no other sector that was negatively impacted in this manner during an unprecedented national crisis.

Greater Incentives Needed

There are c. 2.2m cars on the road in Ireland and electric vehicles represent less than 1% of those. The 2019 Climate Action Plan (CAP) includes a target of 840,000 passenger ECV's on the road by 2030, but the roadmap to get there is not clear. Transport accounts for c. 20% of Ireland's Greenhouse Gas Emissions and cars account for about half of this figure. The Environmental Protection Agency (EPA) recently stated to achieve a 51 per cent emissions reduction from transport by 2030, *"significant new measures will need to be identified and implemented*".

The question is how do we get from selling c. 10,000 ECV's in 2021 to almost 100,000 ECV's per annum in order to reach or exceed the CAP target by the end of the decade? The target could change. Or, perhaps the answer is in the EPA statement – significant new measures are needed. To accelerate the pace of ECV adoption in Ireland, greater government-led incentives for consumers and businesses along with infrastructural investment will certainly be required.

Infrastructure

What came first – the chicken or the egg? The European Automobile Manufacturers' Association (ACEA) recently reported that 70% of all European charging points are based in just three countries: The Netherlands, France and Germany. Outside of Norway, these countries have some of the highest rates of EV adoption. Investment in infrastructure in these markets provides confidence to consumers when purchasing an EV.

There are approximately 1100 charging points around Ireland. The ESB announced last year they will invest €20m to upgrade the existing infrastructure. "A lot done, more to do" comes to mind. As more Irish consumers adopt EV's, accelerated investment will be required by the State to expand the current network, particularly in rural areas to ensure the growth of EV's is not only centred around urban locations.

Outlook

Our outlook remains cautiously optimistic. The Bank of Ireland Economic Pulse came in at in 89.7 in June 2021. The index, which combines the results of the Consumer and Business Pulses, is up 33.4 on a year ago. For those fortunate enough to maintain their employment and income during the health crisis, savings have increased. The sector is likely to experience a bounce as a result. Some consumers postponed taking delivery of new vehicles until restrictions were lifted and this is likely to lead to a strong H2 for vehicle sales. The recovery is expected to continue into 2022.

The agreement of a trade deal is seen as positive in the sector as lower volumes of used imports enable residual values to recover. A reduction in used imports should have an overall positive effect on the new car market over time, as the market here will need to generate more used car sales as supply from the UK slows. Electric vehicle sales are predicted to grow to the region of 10% of new car sales in 2021.

Restrictions on international travel continues to dampen the overall new car market as hire drive sales typically account for c. 15% of the market. Hire drive sales accounted for c. 6% of new car sales in the first half but is expected to improve in H2 as international travel recommences. The Society of the Irish Motor Industry (SIMI) predicts a new car market of c. 98,000 units in 2021 (+11%). This compares to a new car sales of 117k in 2019 and 147k in the peak year of 2016. Due to pent up demand, new car sales are currently predicted to recover to c. 120,000 units by 2022 depending on how COVID and Brexit issues evolve and get resolved.

Aftersales

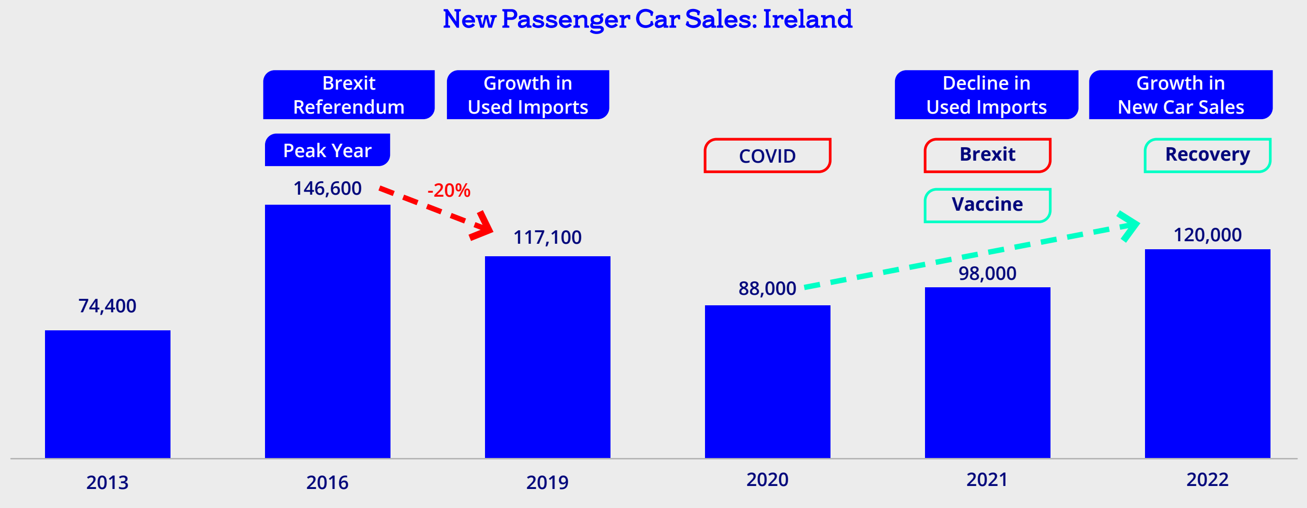
It should be noted that the sector is not just about new vehicle sales. Franchised motor dealers benefit from multiple income channels including used cars and aftersales channels (service and parts). Aftersales channels attract strong margins and can account for c. 40% of total income contribution. Many motor retailers focus on developing profitability in their workshops as this gives protection against volatility in new car sales. A key industry KPI is the Absorption ratio where the benchmark is 80%. A ratio of 80% indicates that direct profit produced from aftersales will absorb 80% of administrative overheads, thus providing comfort to a dealer during times of instability.

Finance Opportunities

We expect that trends existing pre-COVID will carry forward into H2 2021. Consolidation of single operators into larger dealer groups is likely to continue and may accelerate. Refinance opportunities will present themselves from time to time and we welcome the opportunity to discuss these needs with both current and new customers.

Supporting our Customers

Bank of Ireland Finance (BIF) supports 13 motor franchises representing c. 41% of annual new car sales and we remain committed to our customers. Bank of Ireland and the Irish Motor Sector is open for business.



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Stephen joined Bank of Ireland in 2018 and brings over 20 years Motor Sector experience developed in both Retail and National Distributor positions. He comes to us direct from industry having previously been employed as General Manager for a multi-franchised retail motor group for 7 years.

He opened a new retail operation in 2011 in a very challenging economic environment and was responsible for building both Sales (new and used) and Aftersales (Service and Parts) functions of the business. In addition to a first class honours BA in Business Studies (Hons) from Griffith College Dublin, Stephen holds a Certificate in Transport Engineering from Dublin Institute of Technology.

Sources: Bank of Ireland Economic Pulse, Society of the Irish Motor Industry (SIMI), European Automobile Manufacturers' Association (ACEA), Sustainable Energy Authority of Ireland (SEAI), Society of Motor Manufacturers and Traders (SMMT), European Environment Agency (EEA), Department of Transport, Automotive News Europe.