CARMAKERS:

New energy vehicles the clear exception to weaker sales

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The China Automobile Dealers Association's proposal to China's finance and commerce ministries was to halve the 10 percent car purchase tax, in a move to offset sluggish sales.

It is welcome news after passenger vehicle sales — cars, minivans and SUVs — experienced the biggest drop in auto sales in China in seven years in September to 2.39 million units, according to the China Association of Automobile Manufacturers (CAAM).

American brands Ford and Chrysler saw sales drop 13.66 percent year-on-year between January and October. French brands saw their sales drop more than 20 percent.

Domestic Chinese brands, on the other hand, saw overall sales drop by just 3.6 percent year-on-year over the same period. Sales of Japanese and German brands both grew by almost 5 percent.

Chinese automakers sold more than 8 million cars in the first 10 months of 2018 — more than double the sales of second and third place Japanese and German brands, which sold a combined 7.76 million cars — according to CAAM.

The one very visible exception in weaker sales is in NEVs. Fitch Solutions expects electric car sales in China to grow considerably in the coming decade as the government works to combat pollution, said Fabrice Gatwabuyege, an automotive industry analyst at Fitch.

Rising sales of NEVs may be directly linked to rules set in their favor, which also make it more difficult and expensive to secure a permit for a traditional gasoline-powered car.

Chinese automakers like BYD, Chery and Great Wall Motors are rapidly improving their offerings, particularly in electrics and hybrids, which helps them hold on to market share.

Chinese automakers are also looking to tap foreign markets in competition with Korean and Japanese car exporters. Some of China's biggest auto export markets are emerging economies like Iran, Vietnam, Mexico, Peru, Myanmar and India. They are also tapping more developed economies, like Chile and even the United States. In the first quarter of 2017, for example, 6 percent of China's auto exports went to the US.

In June, BAIC Group started exporting electric cars to Mexico to be used as taxis.

As they look to tap foreign markets, China's automakers find themselves competing in a more open field as the country continues to liberalize its giant auto market.

However, even as trade tensions simmer, China continues to liberalize its giant auto market.

A traffic jam during rush hour in Beijing on Jan 17. Foreign carmakers are setting the groundwork to ride the long-term growth of the Chinese auto market.
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Draft Administrative Rules on Auto Industry Investment released in May by the National Development and Reform Commission looked to improve entry standards for investments in the sector, control increases in production of traditional cars, promote NEVs and push for the development of intelligent vehicles.

In September, China increased tariffs on vehicles imported from the US but lowered them for vehicles imported from other countries.

China also issued a new policy that uses credits to encourage the production of EVs and hybrids.

The global auto industry is closely watching the slowed growth in Chinese sales, and some carmakers are adapting to the changes.

US electric vehicle maker Tesla is constructing a $140 million factory in Shanghai. News of the factory and a surprise turn to profitability in the third quarter helped the company's share price jump.

"We believe that by producing cars in China, Tesla will have more direct access to the market, enabling the automaker to quickly adapt to consumer demand. This will therefore better position the American automaker to tap into China's fast-growing market for NEVs," said Fitch's Gatwabuyege.

BMW, for its part, plans to invest $3.5 billion in Chinese factories to step up EV production. BMW also plans to pay $4.2 billion to boost its stake in its joint venture BMW Brilliance Automotive from 50 percent to 75 percent.

These investments suggest carmakers are setting the groundwork to ride the long-term growth of the Chinese auto market.

"Overall, passenger vehicles edged up 0.6 percent year-on-year (in the first three quarters) versus 1.4 percent year-on-year growth in 2017," said Anna Yu, vice-president of oil and gas sector research for ICBC International.

"We believe that weakened sales are mainly due to weakened consumer sentiment amid intensifying China-US trade tension and the slowdown in economic growth."

Trade turmoil has hit Tesla hard, as it now faces an import tariff rate of 40 percent compared to 15 percent for other imported cars in China. Tesla had to raise the price of its Model X and S cars by about 20 percent — an extra $30,000 — for Chinese customers in July.

"By localizing vehicle production, we believe that Tesla will be able to reduce the risks any potential future trade disputes between the US and China would have on its operations in the Asian nation," said Gatwabuyege.

The Chinese tariffs were a response to the original levies imposed by the US.

Major automakers have adopted strategies to cope with the downturn.

Tesla is pushing for more local production. Ford, in turn, is reshuffling Asia-Pacific operations by making Ford China a stand-alone business unit that will allow "greater focus on the market, faster decision-making and increased Chinese leadership".

Gatwabuyege noted other factors for the slowdown that companies must address.

"The slump in car sales this year has been due to the slowdown in growth momentum of the Chinese economy, a weak domestic stock market and market uncertainty as a result of trade tensions between China and the US," he said.

"In addition, new emissions standards, which are set to come into place next year, have also led to consumers postponing new car purchases."

And then there is the natural comedown from the industry's boom of years past. "The car market was also due for correction after some years of significantly high growth," Gatwabuyege said.

Another consideration is the cancelation of purchase tax subsidies on vehicles with an engine size of 1.6 liters or below, ICBC's Yu said. A shrinking pool of auto finance options for consumers after recent crackdowns on peer-to-peer lending platforms may also have stifled demand.

And it is here that domestic manufacturers might see an opportunity. Not only would Chinese manufacturers have a pricing advantage, their production capacity may also help them meet market demand.

"Domestic Chinese companies certainly do look up to the task as they have a wide range of electric vehicles on the market. Foreign carmakers still face a challenge in terms of ramping up production of electric vehicles in China in order to meet the new energy vehicles sales quotas," said Gatwabuyege.

Yu said that domestic automakers currently hold a greater market share of NEV sales in China than their foreign counterparts, citing China's BYD, BAIC and SAIC as examples.

"These domestic automakers are mostly targeting mid- to low-end markets and they have long been building their footprints in China's new energy vehicle market ahead of their foreign counterparts."

Yu believes the opening-up of China's auto industry for foreign companies that already have joint ventures with domestic automakers could lead to tougher competition for domestic brands.

But there is still room for collaboration. Domestic carmakers are building stronger relationships with foreign partners. JAC Motors has a joint venture with Volkswagen focused on electric vehicles, as does Zotye with Ford, and Great Wall with BMW to produce electric Minis.

"With greater control of business, more foreign marquees will be encouraged to enter China's auto market, lifting their domestic production," said Yu.