

Automotive News

Falling used-vehicle values threaten recovery

Used-vehicle prices have slipped for three straight months due to an influx of off-lease vehicles, just as analysts predicted.

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The long-awaited decline in used-vehicle prices has finally arrived, only it may turn out to be steeper drop and a bigger threat to the overall market than almost anyone expected.

Prices have slipped for three straight months due to an influx of off-lease vehicles, just as analysts predicted. But other factors have led to new warnings that are substantially gloomier.

“We see an alignment of forces that could drive the largest decline in used-car prices in history,” said Morgan Stanley analyst Adam Jonas.

Others disagree — strongly — saying the decline will be within the traditional seasonal range.

Either way a lot is at stake.

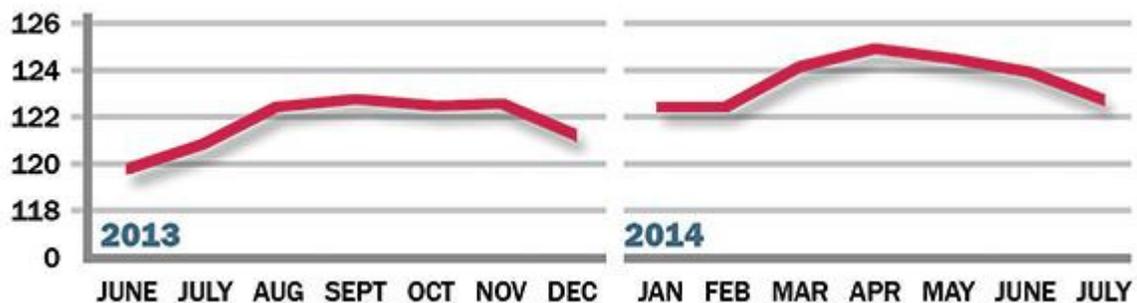
“Used-car prices are probably the single most important metric analyzed when judging the health and well-being of the U.S. auto cycle,” said Jonas.

Strong used-vehicle prices make it more likely new-vehicle shoppers will get a high price for their trade-in and won't be underwater on their current vehicle's loan. If used prices tank that will make [car](#) buying significantly more expensive for many Americans.

Jonas cited several reasons for his dire forecast.

- The Manheim Used Vehicle Value Index declined in July from the previous month for the third month in a row, with prices of used full-sized cars down for 35 straight months.
- The decline came despite what Jonas called a “relatively tight” used-vehicle market, at around 45 days supply.

- Amid widespread offers of 0 [percent](#), 72-month new-car [loans](#), declining new-vehicle transaction prices are putting pressure on used-vehicle margins.
- Jonas' discussions with rental-car companies "suggest a shift back towards program cars," with automakers guaranteeing they will buy back vehicles that are retired from the rental fleet, as opposed to "risk cars," for which the rental companies assume the risk of price depreciation. Jonas called that "a complete U-turn from the direction they were headed just six months ago."



Used prices turn lower

The Manheim Used Vehicle Index fell for the third straight month in July. It measures changed in used-vehicle prices and is adjusted for vehicle make, model and time of the year. January 1995 is the base year of 100.

In the 1990s, automakers loaded the rental fleets with program cars, pushing up the carmakers' sales but severely damaging the vehicles' residual values when those cars had to be dumped at [auction](#) later.

Rental-car companies declined to divulge what portion of their fleets are program cars vs. risk cars. But each of the three companies that dominate the U.S. rental-car industry admits that it still has [vehicles](#) in its fleet that typically it would have remarketed last spring, either sending them to auctions or selling them directly to dealers or consumers.

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Recall delays

Hertz Corp., Avis Budget Group Inc. and Enterprise Holdings all say they had some vehicles that they had to park while awaiting recall-related repairs, postponing those cars' sales. Some also kept cars in their fleets to meet demand from drivers who needed replacements after their own cars suffered damage from severe weather.

Now, those retired [rental cars](#) will have to be unloaded by the thousands this fall, in a market in which used-vehicles are more plentiful and prices already are dropping.

In contrast to Jonas' worries, auction company Manheim, in a commentary accompanying its monthly Used Vehicle Value Index, said the three-month decline in used prices "has prompted talk of a free fall in pricing. That talk is premature."

The commentary noted that the declines reflected adjustments that many thought would have happened earlier in the year.

Although the Manheim index dropped in July, it stood above the year-earlier level. The index measures changes in used-vehicle prices and is adjusted for vehicle make, model and time of year.

Ricky Beggs, editorial director at Black Book, said used-vehicle prices depreciated 4.5 percent in the first six months of 2014 and predicted they will slide another 8.5 to 9 percent in the second half of the year.

'A good year'

But he was quick to point out that the predicted 13.5 percent decline for 2- to 6-year-old vehicles is well below the typical annual declines of 15.5 percent seen before the recession.

"It's still going to be a good year as far as retention values and level of depreciation," he said.

Tom Kontos, chief economist at auction company ADESA, admits used-vehicle prices are under pressure from both the additional supply coming from rental-car companies and from strong new-car sales, which have left many dealers with more trade-ins than they can handle. Those trade-ins are showing up in auction lanes, squeezing used-vehicle prices.

The used-car market also has anticipated a sharp rise in the number of late-model off-lease vehicles. This year, the number of off-lease vehicles will increase by roughly 500,000 units from 2013's level, with most of the increase coming in the second half. Next year, the off-lease vehicle supply will increase by 700,000.

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This year, those vehicles are coming into a "tough" but also "highly resilient" used-vehicle market, Kontos said. He believes the additional out-of-service rental vehicles arriving this autumn, though ill-timed, can be absorbed "without a dramatic" drop in price.

Part of that resilience, he notes, is because franchise dealers' appetite for late-model vehicles is healthy. They need inventory to feed their profitable and growing certified used-vehicle sales.

Industrywide, certified pre-owned sales have grown 9 percent through July and are en route to their fourth straight record year.