Luxury vehicle sales hit 3½-year lows

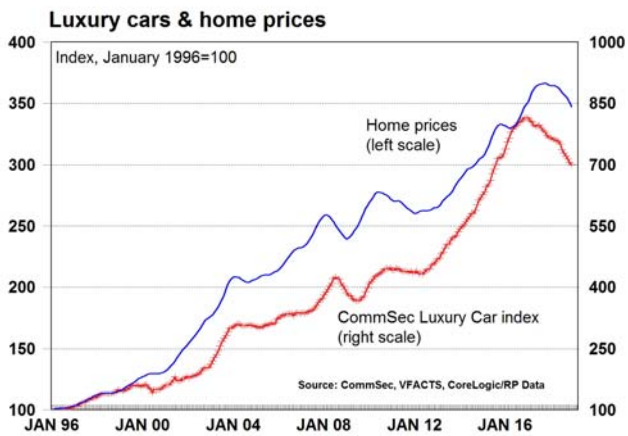
Economic perspective

- **<u>CommSec Luxury Vehicle index:</u> For around a decade, CommSec has been tracking an index of luxury vehicles. Changes at the 'top-end' of markets – vehicles, houses and other assets – have tended to lead activity more broadly. We update the latest trends in luxury vehicle sales.**
- **<u>Luxury vehicle sales:</u> The CommSec index of luxury marques peaked in the 2016 calendar year with sales totalling 106,658 units. In 2017, luxury vehicle sales fell by 5.7 per cent and sales fell by a further 8.9 per cent in calendar 2018. There were 91,642 luxury vehicles sold in 2018 – a 3½-year low.**
- **<u>Home prices:</u> The CoreLogic Home Value Index of national home price index fell by 1.1 per cent in December to be down 4.8 per cent over the year – the biggest annual fall in a decade. Home price growth started to slow from November 2016, around the same time that luxury vehicle sales started to soften.**

The vehicle sales data provides guidance on consumer spending as well as conditions for the Autos and Components sector of the sharemarket.

What does it all mean?

- On September 18 2017, CommSec published a report *"Luxury vehicle sales peak: Omen for homes".* We updated the report on both April 6 and August 7 2018. This report updates recent developments.
- When luxury vehicle sales are in retreat you can bet that home prices aren't far behind. That has been the case since the early 1990s. And indeed that's the case now.
- Vehicle affordability is still at record highs – especially affordability of luxury vehicles. And the job market is strong. But wages are growing at a slower pace, although still outpacing inflation. Also national home prices are now falling, dragged lower by the Sydney and Melbourne markets. And that affects wealth and confidence. So both the new vehicle market and housing market are slowing at the same time. And the 'top-end' of both markets are leading the slowdown. That is not necessarily negative, Aussie consumers may look to spend elsewhere. And indeed growth of retail spending has lifted and a record number of Aussies are taking holidays abroad.



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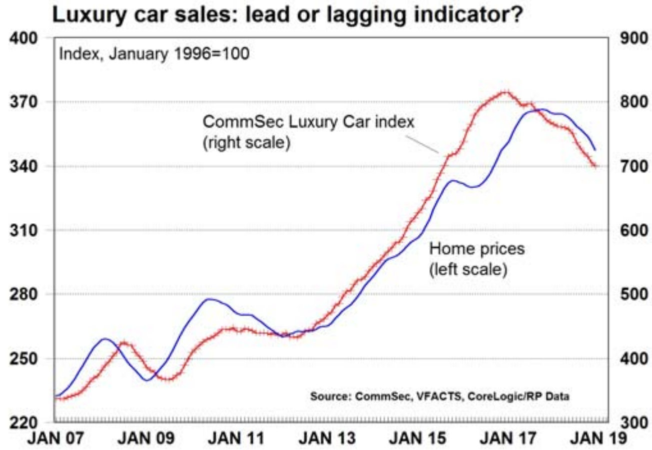
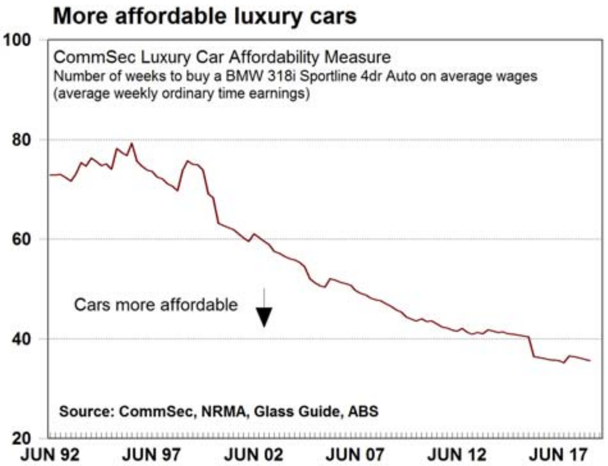
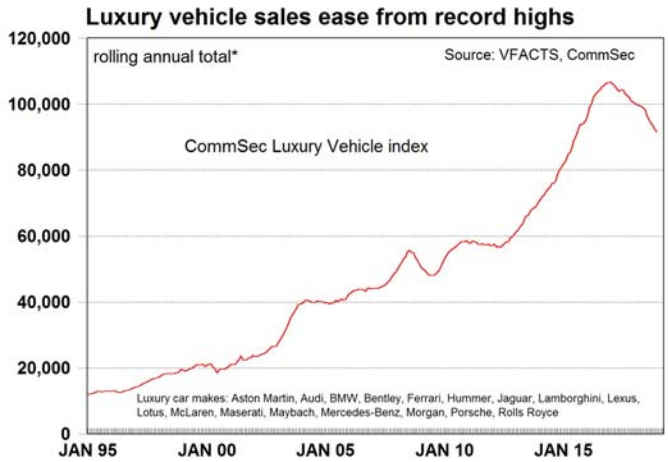


- Quite remarkably, sales of luxury vehicles have tracked movements in home prices over time. Monthly growth of national home prices started to slow in November 2016. After ebbing and flowing in late 2016/early 2017, growth of home prices slowed from mid-year with prices starting to fall in October 2017. The current 1.1 per cent monthly fall in home prices is the biggest in 10½ years.
- The lead-lag relationship between vehicles and homes has shifted over time. In 2017 it was luxury vehicle sales that started to soften ahead of home prices. Double-digit annual gains in luxury vehicle sales had been in place from 2013. But in late 2016 gains in affordability peaked and vehicle sales slowed in line with a lower Australian dollar and stable interest rates.
- Annual sales of luxury marques started falling in early 2017 and home price growth also slowed around the same time. For the first time in 6½ years, home prices are falling in annual terms at the same time that sales of luxury vehicles are falling. In 2013, luxury vehicle sales recovered as the benefits of a strong currency were passed through to buyers in cheaper prices. And both vehicle and home sales lifted from 2013-2016 in response to lower interest rates.
- The question is what will drive the recovery of luxury vehicle sales and home prices in 2019. The Aussie dollar is trading in the low 70s against the greenback, limiting the potential for lower vehicle prices. And interest rates aren't likely to move any time soon. The hope is that the tighter job market will lift wages, in turn boosting vehicle sales and home purchases.

The CommSec Luxury Vehicle index

- According to the Federal Chamber of Automotive Industries (FCAI), new vehicle sales peaked at 1,201,309 units in the year to March 2018. In the period since, vehicle sales have fallen by 4 per cent.
- However, to get a gauge of the luxury market, CommSec tracks the sales of 17 luxury marques: Aston Martin, Audi, BMW, Bentley, Ferrari, Hummer, Jaguar, Lamborghini, Lexus, Lotus, McLaren, Maserati, Maybach, Mercedes-Benz, Morgan, Porsche and Rolls Royce.
- Sales of luxury marques hit peak levels of 106,658 units in the year to December 2016. In the period since, luxury vehicle sales have fallen by 14.1 per cent. Annual sales are now the lowest in 3½ years.
- Clearly luxury vehicle sales have had a good run, tracking the increase in wealth and rising levels of vehicle affordability to their record highs.
- Luxury vehicles now represent 10.5 per cent of all combined passenger vehicle and SUV sales, below the record high of 11.5 per cent set in the year to December 2016. Until late 2016 the proportion of vehicle sales devoted to the luxury market had been steadily rising over time. Despite the recent slowdown, the luxury vehicle market share is double the levels of 13 years ago. Sales of all luxury marques represent 8.0 per cent of all vehicles, down from the record high of 9.0 per cent in calendar 2016.
- Using January 1995 as a starting point (January 1995=100) the CommSec luxury vehicle index stood at 766.4 in December 2018 versus 170.4 for the broader passenger/SUV market. In other words, while passenger/SUV sales are around 1.7 times higher than 23 years ago, the number of luxury vehicles sold has risen seven-fold over the





same period.

- Despite the recent slowdown, luxury vehicle sales are still healthy with rolling annual sales of both Lamborghini and Aston Martin marques at record highs for the 2018 calendar year.

Rising wealth & affordability

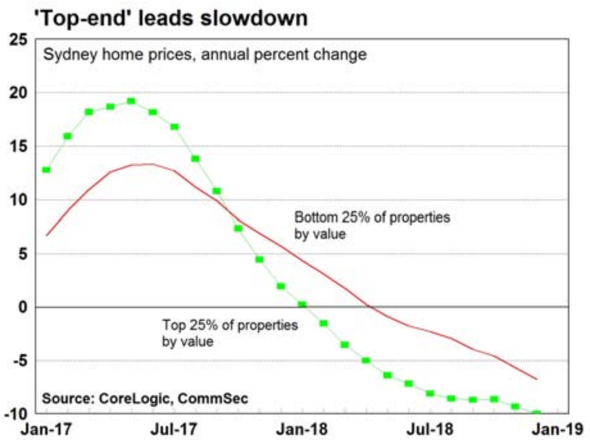
- The increased importance of luxury vehicles in the broader vehicle market is a function of rising wealth levels and better vehicle affordability. In real terms, per capita wealth has almost doubled over the past 14 years, broadly matching a similar increase in the share of luxury vehicle sales.
- Until the past year, Australian wage earners also enjoyed a marked improvement in real wages, that is, wages outstripping prices. Average weekly earnings have risen by 42 per cent over the past decade, ahead of a 24 per cent increase in consumer prices.
- For the new vehicle market as a whole, vehicle affordability has markedly improved in recent years. In fact, according to the **CommSec Vehicle Affordability measure**, vehicle affordability is at the best levels ever recorded. It now takes a worker on average earnings around 21 weeks to buy a new Holden Commodore, down from 28 weeks of wages just five years ago and 32 weeks of wages a decade ago.
- But vehicle affordability hasn't just been improving for the top volume selling vehicles. At the top end of the vehicle market, not only have wealth and real wages been rising solidly, but prices of luxury marques have been flat or falling. And wage earners have been looking to upgrade their rides over time, pushing more sales into the luxury vehicle category.
- Today it takes a worker on average earnings just 36 weeks to buy a new BMW 318i, down from almost 42 weeks of wages just over five year ago.

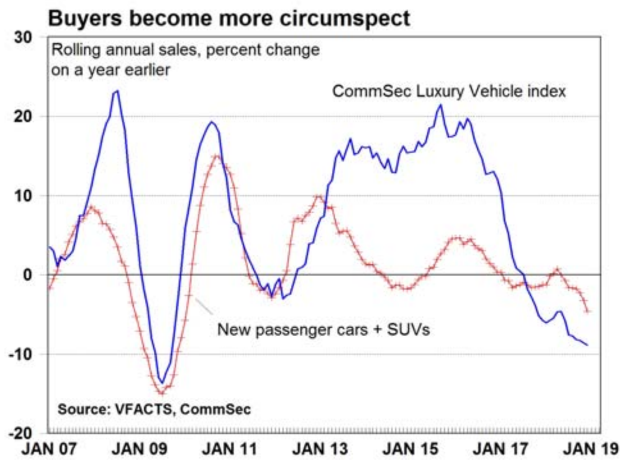
Luxury vehicles, houses & spending: Past cycles

- Over time, luxury vehicle sales have proved useful as an indicator of consumer trends, reflecting their increased importance in the broader vehicle market. In fact, around nine years ago, luxury vehicle sales bottomed in annual terms in July 2009, preceding a more general improvement in the vehicle market by around two months. But the lead-lag relationship has varied over time. Back in 2003, a slowdown in the luxury vehicle market was in evidence around a year before a downturn in the broader vehicle market.
- The slowdown in the luxury vehicle market in 2008 coincided with a peak in the housing market, providing validation for the start of the slowdown. And the annual decline of home prices bottomed out in early 2009, again in line with that of luxury vehicle sales and ahead of the broader vehicle market. Moves by the Federal Government to support building, home sales and home prices were largely successful, also serving to boost consumer confidence and spending.
- While there is a close relationship between trends in home prices and luxury vehicles, around 15 years ago a downturn in the housing market actually led the slowdown in new vehicle sales. That is, the decline in housing wealth led to weaker spending on goods such as vehicles. At that time, the Reserve Bank tightened monetary policy decisively between August and December 1994, causing home prices to flatten over 1995. Luxury vehicle sales then followed the softening of home prices, trending sideways over the 1995/96 financial year.
- The annual growth rate of luxury vehicle sales peaked in December 2009 while annual growth of broader passenger vehicle sales peaked in April. Annual growth of home prices peaked in June 2010.

What is the importance of the economic data?

- The **Federal Chamber of Automotive Industries** releases estimates of **vehicle sales** on the third business day





of the month. The figures highlight the strength of consumer spending as well as conditions facing auto & components companies.

- The **CoreLogic Hedonic Australian Home Value Index** is based on Australia's biggest property database. Unlike the ABS Index, which excludes terraces, semi-detached homes and apartments, the CoreLogic Hedonic Index includes all properties. Home prices are an important driver of wealth and spending.

What are the implications for interest rates and investors?

- The luxury vehicle market soared from 2013-16. Home prices similarly soared in many capital cities over the same period. But now both markets are in consolidation mode.
- The softening of new vehicle sales and home purchases aren't necessarily negative developments. Supply and demand constantly adjust over time. And that is happening now. But the job market remains strong and interest rates are near record lows.
- If fewer dollars are spent on homes and luxury vehicles, consumers may pay more attention to other interests. In 2004 and 2005 when home prices softened and luxury vehicle sales flattened, more Australians travelled overseas. Annual growth of tourist departures was up a record 28.8 per cent in the 2004 calendar year. Indeed the latest data shows that a record number of Aussies are currently travelling abroad.
- Traditional retail spending may also benefit if 'top end' sales activity slows. Aussie consumers may also devote more dollars to spending on services like health, hospitality and education and also look to pay down debt and lift savings.

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