Commentaire Allianz Trade : Electric cars – No price war yet

Deep cuts in battery-electric car prices are reviving fears of a price war in the automotive market. But new car prices show no sign of cooling down in the US. Tesla, the world's largest battery-electric vehicle (BEV) manufacturer, announced another round of substantial price cuts in Europe and North America. Last year, rising new and second-hand car prices (up +7% and +11%, respectively) played a major role in driving headline inflation figures, contributing to the record profits reported by dominant carmakers. Tesla's move, while significant at a micro level, is unlikely to have any substantial impact at a macro level. With about 30,000 cars registered in France in 2022, the company's market share is rising but remains below 2%. Since January 2023, the two rounds of price cuts have brought the bill for entry-level versions of its Model 3 and Model Y down by -10% and -21%, respectively. Factoring in the company's market share, sales mix and the announced priced cuts, and keeping all else unchanged, we find that the announced price cuts would bring down the total French new car price index by just -0.3%. Overall, France recorded a +7.3% increase y/y in March 2023. Applying the same process to the US, we find that lower Tesla prices would have a -0.5pp deflationary impact but overall new car prices still rose by +6.6%.

Other companies see no reason to compete on prices when demand continues to recover: We forecast car registrations in Europe and North America to increase by +4% and +7% in 2023, respectively. A macro impact would be more tangible if competitors were to follow Tesla's example. Applying the same price cuts announced by Tesla not just to the company's cars, but to all battery-electric vehicles sold in France and the US by its competitors, we compute a -2.2% and -0.9% adverse impact on new car prices, respectively – the gap reflecting the much higher penetration of BEVs in France (13%) vs. the US (6%). We find this scenario unlikely. As car registrations have been increasing continuously since August 2022 both in Europe and North America, and order book levels remain above trend, most carmakers can afford minor market-share erosion knowing they will still enjoy rising deliveries. We expect car registrations in Europe and North America to increase by +4% and +7% in 2023, still -27% and -14% below pre-pandemic levels, respectively. Rather than a price war, we expect the progressive rebalancing of supply, which is recovering, and demand, which is expected to soften later in the year, in the European and North American automotive markets to bring car prices back to equilibrium. Finally, input prices, albeit decelerating thanks to the fall in commodity prices, is a welcome yet not sufficient reason to allow for price moderation.

Deep price cuts are a risky gamble for carmakers. Another reason why industry-wide price cuts are unlikely lies in the importance of the residual value of vehicles for private customers: Any drop in price for a given new model has an adverse impact on the resale value of the same models already on the roads, and to some extent on similar models. Past examples of deep vehicle price cuts were met with negative reactions from current customers whose cars immediately lost value, prompting them to think twice before buying from the same brand. The issue is even more critical for specialized car fleet companies since the residual value of their fleet accounts for the bulk of their assets – in this respect, new car price cuts are taking a toll on their balance sheets. It also applies to the majority of carmakers operating in Europe and North America that offer leasing services through their financial services arm, but to a much lesser extent to Tesla, whose sales mix relies more on cash purchases and traditional credit financing.

It's a question of time for battery-electric vehicle prices to adjust downwards as market penetration increases. Finding the right pace to preserve car value but ensure BEVs are becoming more affordable will be a major challenge for carmakers in the coming years. Looking at China, where BEVs account for more than 20% of the market, we observe that prices are going down at a much faster pace as new models are being introduced. Together with competition, it is companies moving down the learning curve (being more efficient in designing and manufacturing BEVs, thanks to accumulated experience), reaching economies of scale (having lower unit costs as volumes go up) and coming up with innovative technologies (emerging battery chemistries, in particular) that will ensure future price parity between internal combustion engine and electric vehicles.