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CAPITAL ACCOUNT

‘Peak Car’ Is Holding Back the Global Economy

Protectionism, emissions controls and market saturation drag down a linchpin of world economy

In its latest World Economic Outlook, the International Monetary Fund estimates the auto sector accounts for 5.7% of global economic output and 8% of world trade. PHOTO: OWEN HUMPHREYS/PA WIRE/ZUMA PRESS

By Greg Ip

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At this week’s biennial Tokyo Motor Show, Toyota Motor Corp. ’s booth didn’t feature any cars its customers can buy. Instead, the company showcased a mobile service that gives you a health checkup, with the slogan: “The star of the Toyota booth isn’t a car—the stars are people.”

There’s a good reason Toyota is shifting focus from individual cars: The global auto market is shrinking. World-wide sales fell in 2018, are expected to drop again this year, and Moody’s Investors Service projects another decline in 2020.

Some forecasters think this is mostly a temporary result of a troubled global environment. But structural headwinds may be more important. Rising trade barriers and stricter emissions controls are making cars more costly just as many countries’ markets have become saturated and alternatives like ride-sharing have sprung up. In the U.S., car sales peaked in 2016; in the European Union, in 2000; and in Japan, in 1990. Emerging markets were supposed to pick up the slack, but they too show signs of plateauing: Sales in the last 12 months are down 12% from mid-2018 in China and 14% in India. "Peak car," loosely defined as a world with all the cars it needs, may be approaching.

This helps explain why car companies around the world are in turmoil despite low unemployment and healthy consumers. Germany's Continental AG , one of the world's largest auto-parts suppliers, announced Tuesday it was taking a €2.5 billion ($2.8 billion) write-down, warning it doesn't expect global vehicle production to improve much in the next five years. General Motors Co. has endured a five-week strike to gain the flexibility to close plants, cut costs and invest more in electric and autonomous cars. In the second quarter, its sales in China, North America, Europe and South America all declined from a year earlier.

Given the industry's outsize influence, an enfeebled auto industry poses a little-realized risk to the world. In its latest World Economic Outlook, the International Monetary Fund estimates the sector accounts for 5.7% of global economic output and 8% of world trade. The IMF thinks autos contributed a fifth of last year's slowing in global gross domestic product and a third of the slowdown in trade.

When the sales slump began, "people thought this would not last as long as it has," Gita Gopinath, the IMF's chief economist, said in an interview. The headwinds "seem more durable than we thought."

The auto sector is a major customer of steel, aluminum, copper, rubber, plastic and electronics—and pays well. It is also politically sensitive, one reason President Trump has raised barriers to imports. Those barriers and retaliatory actions by other countries are raising costs and cutting into profits.

Bottlenecks in meeting new emissions certifications have delayed the rollout of new models in Western Europe. Meanwhile the European Union is mandating that fleetwide carbon dioxide emissions drop 20% by 2021, according to Arndt Ellinghorst, an analyst at Evercore ISI. The necessary technology, he wrote in a recent report, will add €800 to €5,000 ($890 to $5,560) to a vehicle's cost, or 5% to 11% of the selling price of a car made by BMW, Daimler or Audi. Even if the price ultimately rises only 2% to 5%, that will cut sales by 2% to 5%, Mr. Ellinghorst estimated.

Manufacturers "will have to sell cars that have never been sold in scale before," he wrote. They will have to raise prices in mature markets in which customers are extremely price sensitive, he said, "and if they don't succeed, draconian penalties loom."

While Europe is an extreme case, similar risks hang over many other markets. India has ordered its industry to meet tough new developed-country level standards for emissions of particles and nitrous oxide by next year, potentially raising significantly the price of a car in a market where customers are extremely price-sensitive.

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Innovation typically makes a product cheaper or better. Such isn't the case with cars equipped with technology aimed at reducing emissions like carbon dioxide. Electric cars, for example, are more expensive and have to be recharged—a benefit for the environment, but not the consumer's wallet.

Compounding the rising costs of protectionism and emissions regulations is saturation in developed markets where populations are past their peak car-buying years.

Sales in India and China are suffering payback for excessively easy credit that enabled marginal buyers to buy cars. In China, a sales-tax cut aimed at boosting ownership was reversed in 2017 and 2018.

Michael Dunne, chief executive of ZoZo Go, a consultant specializing in the Asian automobile market, says China, a country of 1.4 billion people, ought to be far from saturation. But most Chinese who can afford a car are clustered along the eastern coast in major cities, "and those city markets have largely become saturated." City governments restrict new car registrations, while electric cars are losing their subsidies. The cost and hassle of owning a car mean many affluent urban Chinese own just one and use a ride-sharing service in place of a second, Mr. Dunne said.

Car ownership tends to rise with per capita income; so as incomes in poorer regions converge with those of richer places, sales should rise. But that process isn't happening "at the speed we thought, so the demand for durable goods like cars hasn't come about," said Ms. Gopinath. The average Brazilian was 77% richer than the average Chinese in 2008 but after a decade of stagnation is now 16% poorer. Not surprisingly, Brazilian automobile sales peaked five years ago.

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