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Driving to Recession and Recovery

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Americans love automobiles. The symbiotic relationship between American business cycles and the automotive industry (specifically, auto and light truck sales) is evident in the chart. Automobiles, as durable goods, reflect both households' and firms' anticipations of future economic activity and automakers' contributions to that activity through spending on physical plants and equipment. Hence, disentangling causal relationships by statistical methods is difficult, if not impossible: The relationships depend on the important role of unobservable expectations of future economic activity. Further, since automobile and light truck sales are durable goods sales, they depend even more than nondurable goods sales on expectations of future economic activity, including uncertainty regarding monetary policy.

Most analysts regard increases in automobile and light truck sales as an important component of an economic recovery. Vehicle sales have been a bright spot during the tepid rebound of the American economy from its 2009 trough. During the first six months of 2012, the annual sales rate for automobiles and light trucks was 14.8 percent higher than during the comparable year-earlier period. During May, news organizations reported that major automobile analysts, including J.D. Power and LMC Automotive, had increased their projections of sales during 2012 to 14.5 million units, a 13 percent increase from 2011.

The automobile sector experienced an epic collapse during the 2008-09 financial crisis and recession. As the chart shows, the annual sales rate started to decrease during 2005-06, coincident with the slowing, and eventual end, of house price appreciation and weakness in equity prices that affected household wealth. Vehicle sales collapsed during the fourth quarter of 2008 and the first quarter of 2009—a period when even potential buyers with good credit were unable to obtain financing. Within a year, vehicle sales slipped 40 percent, to a 9 million unit pace during February 2009 from a 15.5 million unit pace.

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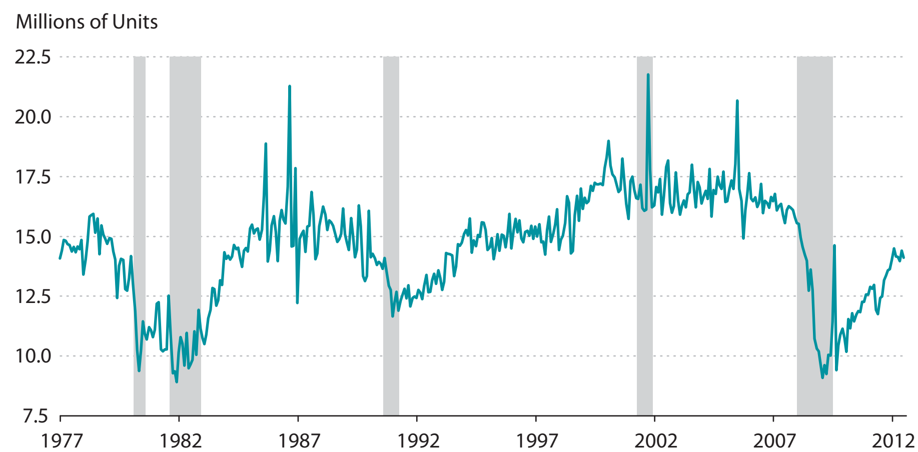
Because fixed costs (for both labor and physical plants and equipment) dominate the automobile industry's cost structures, a 40 percent decrease in revenue portended bankruptcy for auto manufacturers irrespective of the quality of their products or their future viability. To forestall a likely decade-long period of unemployment for displaced workers, the Treasury and Obama administration

Lightweight Vehicle Sales: Autos and Light Trucks



NOTE: Shaded areas indicate recessions as determined by the National Bureau of Economic Research.
SOURCE: Bureau of Economic Analysis/Haver Analytics.

advanced funding, subject to collateral, to auto manufacturers and auto-focused finance companies. As of mid-August 2012, the Treasury reported to Congress that the eventual net cost to taxpayers might be as large as $25 billion.[1]

Since the 2009 sales trough, new car and light truck sales have gradually climbed higher. Most recently, however, slower vehicle sales have mirrored the generally slowing pace of U.S. economic activity, with the July sales rate less than June's. For July, both General Motors and Ford reported lower sales than during the previous month; Toyota and Honda reported stronger sales, as tsunami-related supply-chain disruptions eased. Volkswagen reported a 27 percent increase in sales and announced an expansion at its recently built Tennessee plant. Sales likely also were influenced by fuel costs, as sales of light trucks decreased and sales of automobiles increased. Yet, July sales of 1.15 million vehicles were 8.9 percent better than the same month in 2011. Recent increases in vehicle sales, perhaps, are a signal that the confidence of households and firms is beginning to return. ■

Note

[1] An overview of most federal assistance programs during 2008-09 is provided by Richard Anderson and Charles Gascon in "A Closer Look: Assistance Programs in the Wake of the Crisis," Federal Reserve Bank of St. Louis *Regional Economist*, January 2011, pp. 4-10; http://stlouisfed.org/publications/pub_assets/pdf/re/2011/a/bailouts.pdf.

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