AutoTrader

Market Report

Has the finance bubble burst?

March 2018


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01

Introduction

Nathan Coe
Chief Finance Officer and Chief Operating Officer, Auto Trader

Welcome to the fifth Auto Trader Market Report, a biannual review of the UK's new and used car market, consumer buying and selling behaviours and data taken from Auto Trader, the UK's largest digital automotive marketplace.

This Report comes at a time when there has been increasing doubt and negativity regarding the automotive industry, whether it's the performance of new car sales, the debate around diesel vehicles, or questions as to the sustainability of car finance given its strong growth in the past few years.

The most recent scrutiny stems from that strong finance growth, leading to a simplistic conclusion that it looks like a credit bubble. However, this does ignore the degree to which automotive finance is replacing other forms of finance that were previously utilised, such as mortgage drawdowns and unsecured personal loans. Therefore, the growing cynical view in the City that car finance is a credit bubble waiting to burst is simply not warranted.

The negative outlook on car finance has also largely been based on the expectation that used car prices will crash as a result of an influx of cars entering the market, driven by the growth of new car Personal Contract Plans (PCP). However, we have seen no evidence of this in our price observations despite the new car market growing dramatically since 2012. The average price of a second-hand car on a like-for-like basis increased by 4% between 2016 and 2017.

Despite this evidence, we know that credit markets can be influenced by speculation and media coverage, and as with the diesel debate, we have seen the damage that widespread media coverage can have on car buyer behaviour and the £77.5 billion automotive industry which is a large contributor to the UK economy and employment. For this reason, we believe that a balanced and factual dialogue is crucial when it comes to vehicle finance.

Key industry figures have commented in light of this debate that car finance is conservatively modelled and asset-backed, making it lower risk and unlikely to cause a shock to the financial system. It is also worth noting that the financing of the UK car market operates very differently to other markets like the US, where there are possibly more valid concerns regarding automotive finance.

The Bank of England recently commented that arrears rates on car loans are lower than other forms of credit and therefore present less risk to the lender, which is often the captive finance arm of the manufacturer and not the retailer. PCP agreements account for the majority of new car financing in the UK, and are most prevalent in the top two income quartiles of households. Furthermore, PCP agreements in the UK are most often taken over a 2-4 year period, which is significantly lower than typical finance periods that are often twice the length.

The truth is, automotive finance has been a key enabler to a change in the way people own cars, moving from paying upfront to paying on a monthly basis, a consumer trend that has played out in many retail categories including music, video and mobile phones, to name a few. This shift has already taken place in new cars. In 2017, 88%[1] of new cars were financed by members of the Finance and Leasing Association (FLA), which lent close to £19 billion to private individuals buying new cars. This is a 175% increase on 2011[2]. However, this is only in its earliest stages for the used car market, where only c.30% purchase cars in this way.

We believe that as more finance options on used cars are made transparent online, as we have done on Auto Trader, more and more used cars will be bought this way which represents a good outcome for both car buyers and retailers alike.

The key role finance has played in the UK can be seen when we look at the UK car parc. Ten years ago, there were 31 million cars in the UK. This is now 35 million cars and growing, meaning significantly more people are now able to benefit from car ownership. This general growth in the car parc and the significant increase in younger used cars, all points to supporting factors that signal automotive finance will play a bigger, not smaller, role moving forward.

This is the opportunity for the used car market in 2018. Making the financing of used cars more competitive, accessible and easier to understand for car buyers will be crucial to making more cars more affordable to more people. This will improve the options and choice for car buyers and at the same time increase sales for car retailers.

Our study of 4,000 car buyers revealed that currently 52% consider the price of a car as a monthly figure, rather than the full advertised price. This number will certainly increase, but the rate at which it does depends on how effectively the used car market makes finance tools and offers more attractive and accessible for consumers at the beginning of their car buying journey.

2017 was a year when the public debate in relation to diesel confused car buyers and led to a change in buying that was counterproductive for the market as a whole.

Those who hold influence with car buyers should be careful not to make the same mistake with the finance debate, as finance is arguably the single most important thing for future market growth, as well as the adoption of electric vehicles. Without attractive finance deals, the adoption of electric vehicles will be far slower than the government hopes.

> The growing cynical view in the City that car finance is a credit bubble waiting to burst is simply not warranted

1. The Finance and Leasing Association, Consumer Car Finance (February 2018)
2. The Finance and Leasing Association, Consumer Car Finance (February 2012)

Key findings

59%

of recent car buyers who chose not to go electric say it's due to the upfront expense of electric cars

68%

Car buyers spend 68% (£6,900) more on the sticker price of a car when bought on finance than when bought outright

23%

Just 23% of those buying on finance identified APR as an important consideration when choosing finance

82%

of car buyers purchasing on finance keep within their set budget

61%

of car buyers said that Brexit has had an impact on their car buying behaviour

£200

is the most popular monthly search price on Auto Trader

36%

of car buyers that purchased on finance did so because they couldn't afford to purchase a car otherwise

A market faced with challenges

03

In early January the Society of Motor Manufacturers and Traders (SMMT) confirmed what most in the industry had been expecting that 2017 marked the first annual decline for the new car market in five years, falling 5.7%.[3]

However, contrary to some of the negative commentary that followed the news, the market remains in good health; despite the slowdown, 2017 represented the industry's third best performance in a decade. Not bad for a market that faced unprecedented challenges last year, including the economic uncertainty created by the UK's EU Referendum decision, the demonisation of diesel, as well as an increased focus on profitability over volume by certain manufacturers fuelled/ challenged by the negative trend of sterling impacting their imports to the UK.

The used car market also faced some of these same challenges resulting in a slight fall of -1.1% in 2017[4]. With c.55 million cross platform visits each month, Auto Trader's marketplace offers an accurate picture of consumer buying intentions. Our data highlights just how negative an influence the government's anti-diesel rhetoric had on consumer buying behaviour throughout 2017.

On average, 22% of all searches that take place on Auto Trader each month are based on fuel type. In November 2016, the same month the London Mayor, Sadiq Khan, first made a call for a nationwide scrappage scheme, diesel accounted for 71% of all fuel related searches, while petrol was just 26%. From that point forward, as the anti-diesel rhetoric gathered pace, we saw the number of diesel searches steadily decrease, falling to a low of 54% in December 2017; it has remained at these levels since.

As the number of diesel searches has fallen, petrol has steadily increased its share, rising to an historic high of 43% in January 2018.

However, it wasn't all bad news for diesel in 2017. Despite its declining desirability, used diesel prices are retaining their value. In fact, the findings from the Auto Trader Retail Price Index,

> Contrary to some of the negative commentary, the market remains in good health; 2017 represented the industry's third best performance in a decade

which combines and analyses data from c.500,000 trade used car listings every day, as well as additional dealer forecourt and website data, show that the price of second hand diesels are growing. On average a used diesel cost £14,405 in January, a healthy £777 increase on the same period in 2017. On a like-for-like basis, this represents a 3% year-on-year growth.

3. Society of Motor Manufacturers and Traders new car registrations, January 2018
4. Society of Motor Manufacturers and Traders used car transactions (Q4 February 2018)

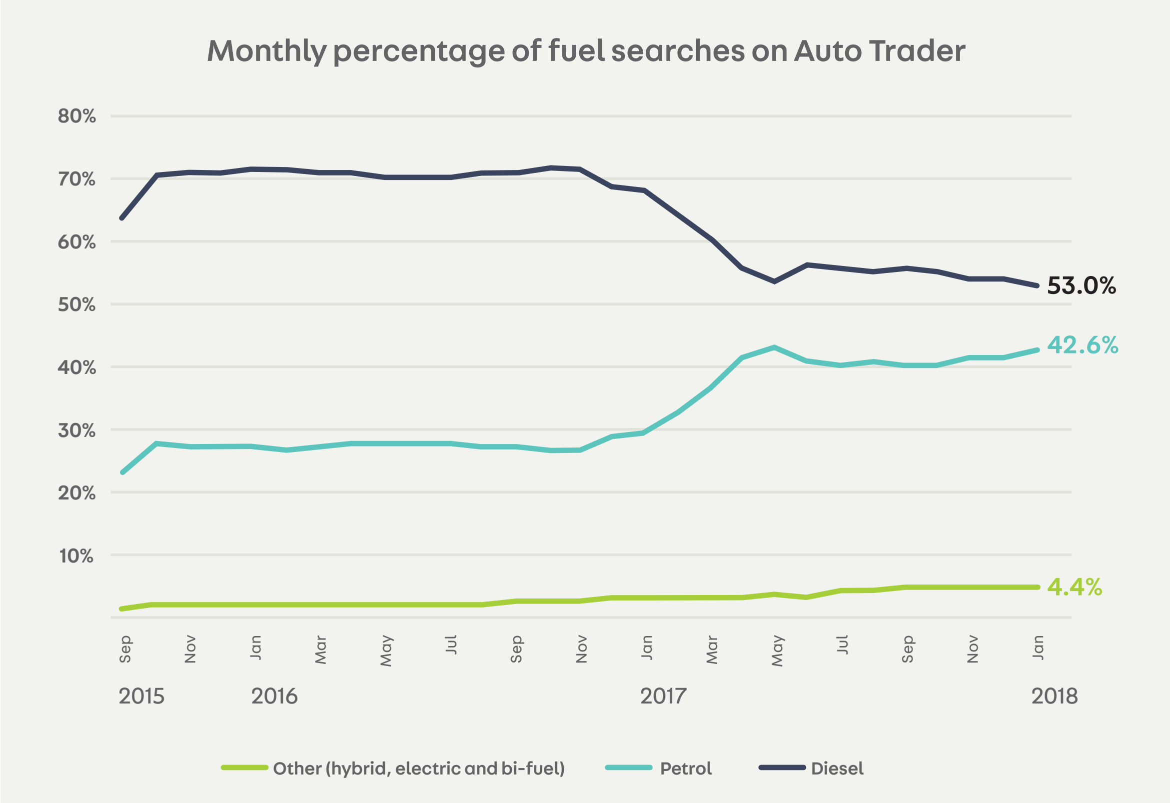
Meeting the government's electric targets

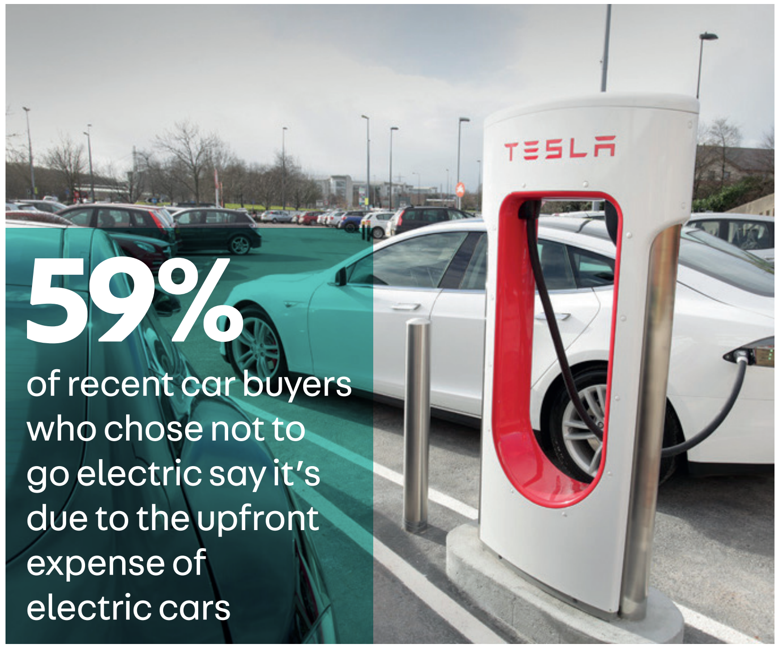
There is little doubt that the tone of the fuel debate has had an extremely detrimental effect on the new and used car markets; the anti-diesel rhetoric is a key factor for the current new car market decline. Not only has it cost the UK economy billions of pounds, creating doubt amongst consumers has also unfortunately undermined the government's green air ambitions. As Mike Hawes, Chief Executive of the SMMT, highlighted: "confusing anti-diesel messages have caused many to hesitate before buying a new low emission diesel car. Keeping older vehicles on the road will not only mean higher running costs but will hold back progress towards our environmental goals."

In January of this year, the Committee on Climate Change warned ministers that three-fifths of new cars must be electric by 2030 to meet greenhouse gas targets. Whilst it applauded the government for its ambitions, unless it does more to turn pledges into reality, it'll fall short of its admirable targets.

If alternatively fuelled vehicles (AFV) are key to its ambitions, the government's approach has been at best a counter-intuitive one. The strategy of criticising diesel (rather than promoting electric) has largely encouraged consumers to either choose petrol (which in many cases is more harmful than modern Euro6 diesel technology), or simply not buy at all. On Auto Trader, AFVs - hybrid, bi-fuel, petrol ethanol, LPG, electric - currently represent just 4% of fuel related searches, but when measured in terms of total volume of searches that consumers are performing, AFVs increased a significant 65% between 2016 and 2017, with electric alone recording a huge jump of 84% in searches.

Whilst consumer interest is growing, there is a need to





focus on motivating motorists to make the move from fossil to electric; dramatically increasing the 119,821 AFVs registered in 2017, which requires greater financial incentives and serious investment in enabling infrastructure. If this was already in motion, we may well have seen a much better result from the diesel debate; rather than car buyers slowing down purchases overall, AFVs could have materially offset the -17.1% fall in new diesel registrations.

Whilst the cost of electric vehicles is decreasing, they remain on average more expensive than their fossil fuelled counterparts and therefore prohibitive to many car buyers. Research for this Report revealed that 59% of recent car buyers who chose not to go electric said it was due to the upfront expense of electric cars.

Ironically, the more government and industry can work together to help make these vehicles more affordable, a key component of which will be attractive finance options, the quicker we will be able to overcome one of the key hurdles to migrating to AFVs.

Finance has the potential to be the key enabler for mass consumer adoption of electric vehicles. Clearly infrastructure and consumer anxieties related to range and efficiency need to be addressed as well, but if attractive finance deals aren't offered then consumers just won't change.

The Brexit effect

Looking ahead, it's hard to predict the extent which these factors will contribute to the health or decline of the automotive retail sector, but the SMMT has forecast a similar performance in 2018, with the new car market expected to fall -5.6[5]. The second-hand market which is always more resilient will perhaps see a similar level of decline to 2017, not least due to the reduced supply of part-exchanges on new car purchases.

As we edge closer to our official withdrawal from the EU on 29 March 2019, the economic uncertainty surrounding it will become increasingly influential on consumer buying behaviour. Our research showed that 61% of consumers said that Brexit has had an effect on their car buying/selling behaviour, with 67% claiming that it had impacted their personal finances. In a wider context, 86% believe Brexit has impacted the overall UK economy.

61% of car buyers said that Brexit has had an impact on their car buying behaviour

5. Society of Motor Manufacturers and Traders UK new car and van registrations forecast - January 2018

The year of used, the year of finance

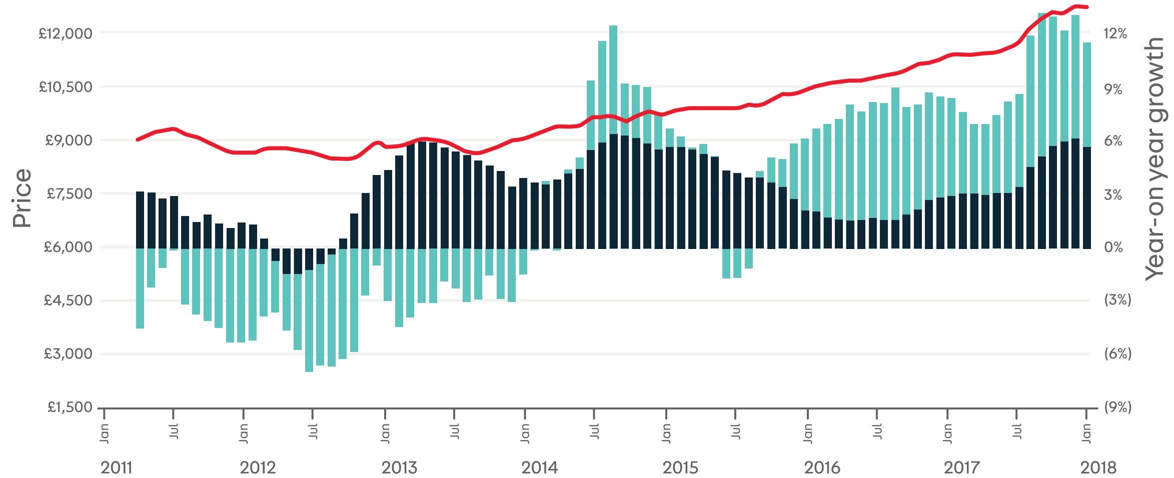
Despite these challenges and changes within the market, 2018 holds some exciting opportunities for both retailers and manufacturers, particularly within the second-hand car market. The number of younger vehicles in the second-hand car parc has grown significantly, driven by the typical three-year renewal cycle. We can see this trend on our own marketplace; in January 2013 approximately 69,000 cars advertised on Auto Trader were aged between 2-4 years old. As of January 2018, that figure is closer to 93,000. Research we conducted last year highlighted that at the start of their buying journey 75%[6] of consumers are open to buying new or used; with younger, better conditioned cars (with more modern options) available, many of these buyers are likely to be tempted to choose recent second-hand cars over new ones. That trend could be helped further by retailers who provide consumers with the reassurance of approved used car schemes where multi-point vehicle checks and extended warranties offer similar peace of mind to a new car purchase.

Naturally, the younger the car the more expensive they'll be - our Retail Price Index showed that the average price of a used car was £11,819 in 2017, which on a like-for-like basis, was a 4% increase on 2016. It's here finance will be key. Not only will it make younger and more desirable used cars more affordable for a wider audience, but the flexibility and convenience of modern finance plans, such as PCPs, will make it a more attractive purchasing option than paying upfront.

However, for retailers to capitalise on this opportunity, they need to evolve their second-hand PCP offers in line with new. New car finance is clear, transparent and easy for consumers to understand. In contrast, the used car finance journey is less clear, typically involves a higher APR, and very often isn't transparent online where car buyers do most of their research.

Our Retail Price Index showed that the average price of a used car grew 4% on a like-for-like basis between 2016 and 2017

Auto Trader Retail Price Index (all vehicles)



Will the finance bubble burst?

In terms of new car market stimulation, the PCP boom is certainly easing, but the bubble has far from burst. There has been increasing speculation that the ubiquity of car finance could have negative consequences for the economy. Some commentators are concerned that to hit high volumes, lenders have made credit acceptance easier, thus making PCPs more readily available to those with less than perfect credit records – and unable to fulfil their commitments like the sub-prime housing market in the US.

Other concerns include the impact of the massive increase in end-of-contract cars hitting the second-hand market, placing too much pressure on what is already a delicate eco-system, the effect of which will dramatically decrease the price of used cars. However, as per our Retail Price Index, there is absolutely no evidence of this on our marketplace.

Manufacturers and industry bodies have been keen to point out that drawing comparisons with the housing market, along with other forms of consumer credit, is incorrect. Unlike housing, where prices can go in any direction, the value of cars can generally only go down, and in a relatively predictable way. As a result, manufacturers assess the risk very carefully and are conservative in their outlook, offering PCPs with a buffer to safeguard against a fall in car prices.

PCP arrangements in the UK differ to those in the US as they are often taken over shorter time periods, but importantly they aren't associated to a sub-prime consumer lending base and therefore aren't associated with the same level of risk as other lending facilities. What's more, PCPs are backed by assets, the cars themselves, unlike many forms of consumer lending. The suggestion retailers have built a false economy for themselves is an inaccurate one.

Another crucial factor is one highlighted by the Governor of the Bank of England, Mark Carney, because unlike most products bought on credit, he said that "people need their cars in general" so are more likely to keep making repayments. Our research for this Report strongly reinforces this point. When it comes to buying on finance, consumers are not overstretching themselves, and the large majority are keeping within their set budget. In fact 82% of car buyers purchasing on finance keep within their set budget.

The rise of PCP

Adrian Dally
Head of Motor Finance, Finance and Leasing Association

The way we pay for our cars has changed considerably over the last decade or so. In 2006, 46% of all private new car purchases were made using dealership finance – now it's 88%.

UK drivers are increasingly focused on usage rather than ownership, and point-of-sale motor finance supports this trend with a range of products to suit those who still want to own the car outright, those who just want to have use of it, and those who haven't quite decided yet.

Traditional loans don't offer that kind of flexibility. In addition, Personal Contract Purchase (PCP) and Hire Purchase (HP) are secured types of finance, and the reduced risk to both the lender and consumer is reflected in the highly competitive pricing which characterises this market. Consumers also benefit from higher levels of legal and regulatory protection – many of which are not available with unsecured loans – including the ability to hand the car back.

PCP has been the market leader for consumer new car purchases for some time, but in 2017 it finally took the top spot in the consumer used car market too, with 49% of consumers choosing it, just above 47% for HP.

The increasing preference for motor finance has changed the motor market – not least the role of dealership staff, who now advise customers on suitable finance products. In recognition of this fact, lenders have been investing heavily in training for the last ten years to help develop and professionalise dealership responsibilities.

PCP has been the market leader for consumer new car purchases for some time, but in 2017 it finally took the top spot in the consumer used car market

Finance fuelling the markets

04

It's undeniable that finance has changed car buying as we know it, with more change expected in light of the continued growth of financing new and used cars. But this kind of change does not occur without significant consumer demand.

Auto Trader's March Market Report for 2017[7] revealed that 98% of car buyers who bought on finance claim to 'own' their car, which highlights how finance has greatly improved the options and opportunities available in the car buying journey but done little to change our idea of car ownership. Similar to mortgages and the financing of other big-ticket items car financing has made the unaffordable, affordable, but the shortening of ownership lifecycles stimulated by finance agreements has also made the used cars we own younger, better conditioned and ultimately more expensive.

Consumers using finance typically pay 68% more on the sticker price of a car than consumers buying theirs outright. The average price of a car bought on finance is £17,087, compared to £10,142 for the average listed price of a car being bought with cash. The price difference between cars being bought in cash versus finance varies greatly depending on a number of factors, some circumstantial, such as the key purchase driver, but there are also some clear spend differences across the age brackets and even regions throughout the UK.

37% of car buyers claim to have bought on finance because it enabled them to spread out their payment monthly

Consumers using car finance typically pay 68% more than consumers buying their car outright

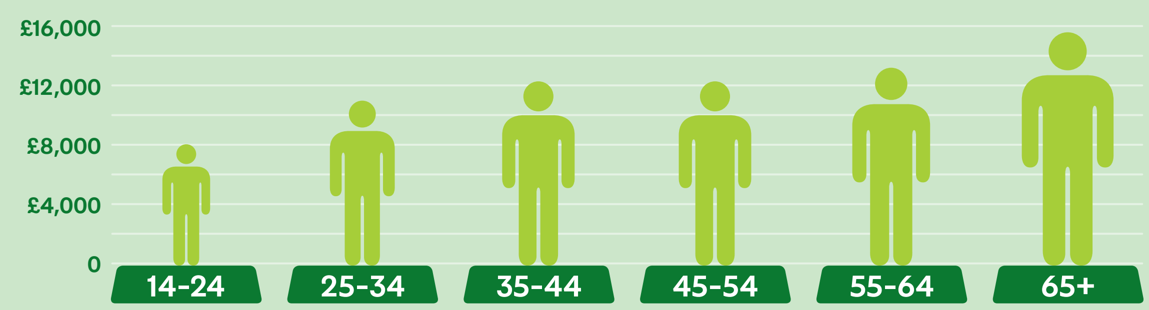
7. Auto Trader Market Report September 2017 https://trade.autotrader.co.uk/market-report/

Is Britain on a budget?

37% of car buyers claim to have bought on finance because it enabled them to spread out their payment monthly, but with almost half (43%) claiming they don't keep track of their household spending, how do consumers buying on finance define a budget that they know is suitable?

The most popular price bracket used to search for cars on Auto Trader through our monthly price search tool is £200[8], with the most popular term length of 36 months. In comparison to the other 5-8 direct debits that consumers have on average a month, car finance payments are one of the more expensive outgoings each month, so it's not

Average car expenditure by age



8. Data taken from Auto Trader marketplace January 2018

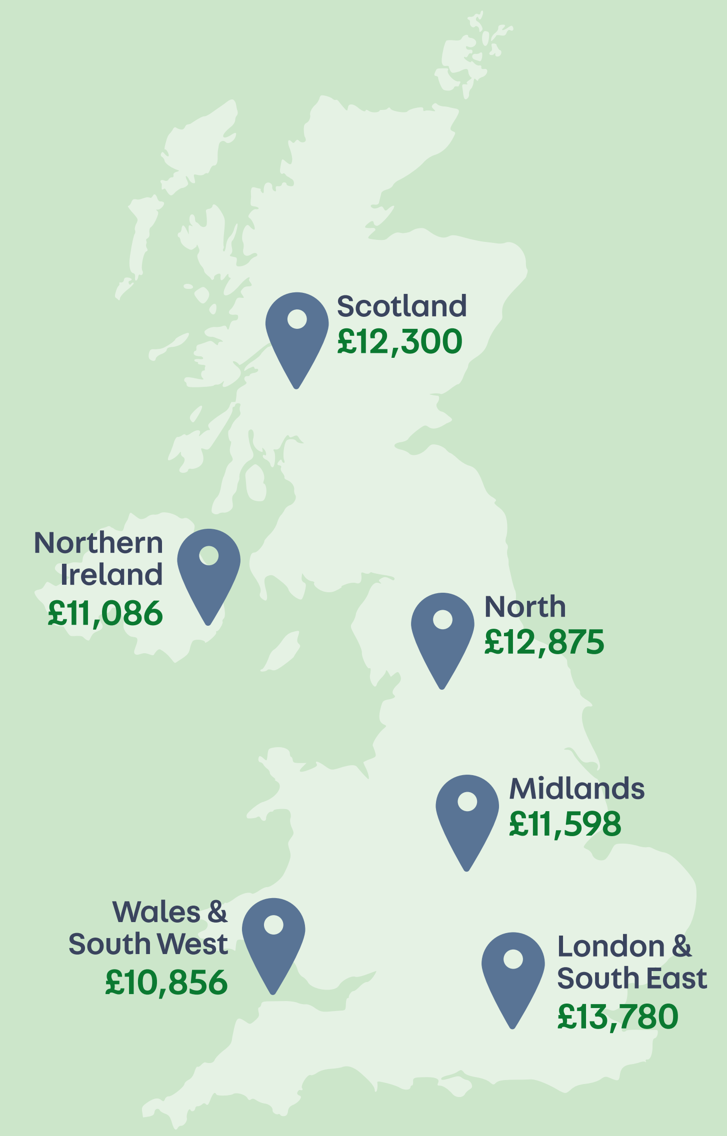
surprising that during times of economic uncertainty, concerns about the cost of car ownership increase.

Research conducted for this Report revealed, that when asked how concerned they were about their personal finances in the current economic climate across a number of monthly expenses, 48% said they were most concerned about utility bills, followed closely by the running of a car (46%). This dropped to 39% for mortgage or rent payments and lower still for job security (32%). This is surprising, considering that in most cases, monthly mortgage and rent costs are far higher than the monthly cost of running a car, and job security is arguably the foundation for ensuring all these payments can be made on a monthly basis.

But despite nearly half of consumers admitting they do not keep track of their household budget and an increasing concern for the cost of car ownership, over three quarters of recent car buyers (82%) agree that their car spending was within the budget they set for themselves.

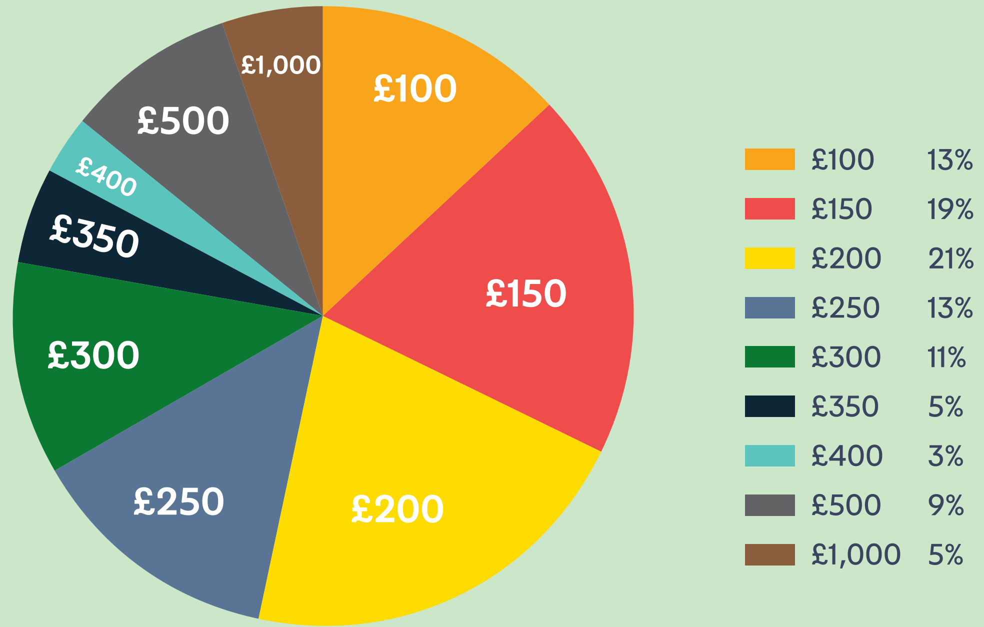
86% of consumers who recently bought a car on finance claimed that the car they purchased was either below or on budget. Those aged 17-34 are significantly more likely to buy a lower spec car in order to stay within budget: 75% which drops to 64% for buyers aged 55+. Similarly, 17-34 year olds are also the age group most likely

Average car expenditure by region



86% of consumers who recently bought a car on finance claimed that the car they purchased was either below or on budget

Monthly price search brackets chosen on Auto Trader



52% of consumers starting the car buying process already claim to consider the cost of a car as a monthly price, rather than the full retail price

to compromise on certain features in order to bring their purchase price down (83%) compared to 70% of 55+ year olds.

And when it comes to researching the finance options available to establish these budgets, only 7% of recent car buyers using finance admit that they did not spend any time researching, with 58% of car finance buyers claiming to have done significant research into their car finance options.

Currently, more than half (52%) of consumers starting the car buying process already claim to consider the cost of a car as a monthly price, rather than the full retail price. With 88% of the new and approximately just 30% of the used car market bought on finance, there is clearly room for growth of finance uptake among consumers; especially as a consideration at the very beginning of the car buying journey which could influence their decision to purchase with finance over cash.

The appeal of finance

05

Finance is a great enabler of affordability when it comes to ownership. Our study of 4,000 consumers showed that 36% of those who purchased on finance did so because they couldn't afford to buy a car otherwise. Highlighting the opportunity for marketers, of those that 'needed' to use finance to afford their new car, close to half (46%) made the purchase off the back of a lifestyle change, such as a new job, a new baby, or getting married.

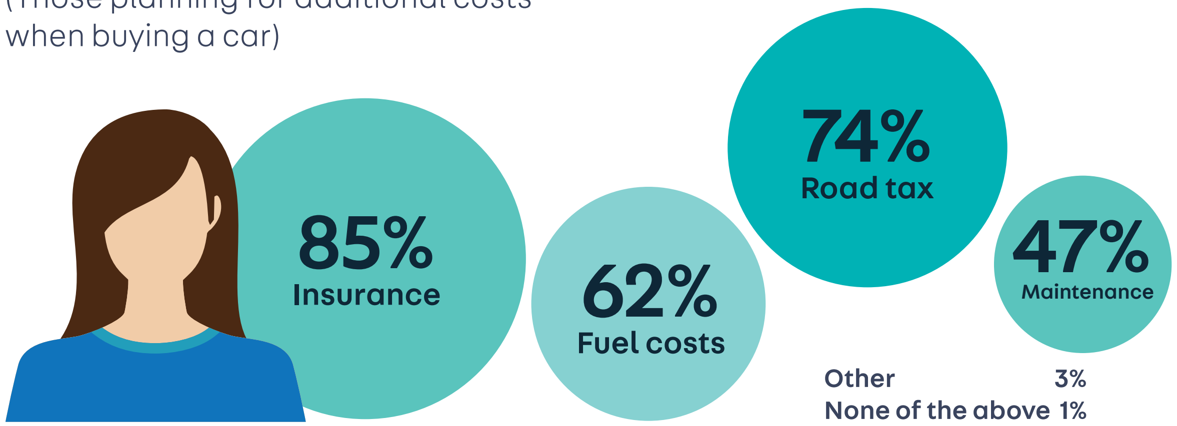
Our research also produced some valuable insight into what key factors influence a car buyer on one finance deal over another. The headline monthly payment cost was by far the most important factor in choosing a finance plan, with 71% of car buyers selecting it as a key decision factor. This was followed by the agreement length (40%) and the deposit length (37%). When we split the findings by age, younger buyers prioritised the length of agreement far more than older drivers; 48% of under 35s versus just 39% for over 35s.

Perhaps most surprising is the lack of significance that car buyers place on annual percentage rates (APR). We know that many manufacturers invest a huge amount of time in deliberating over the level of APR, scrutinising the potential impact the movement of a single decimal point in either direction may have. However, less than a quarter (23%) of car buyers buying on finance consider APR as one of the most important elements influencing their decision, with over half (53%) conducting little or no research on rates. In terms of gender split, women (20%) are less concerned than men (27%). In short, they're far more likely to be influenced by the headline monthly rate cost itself rather than the APR.

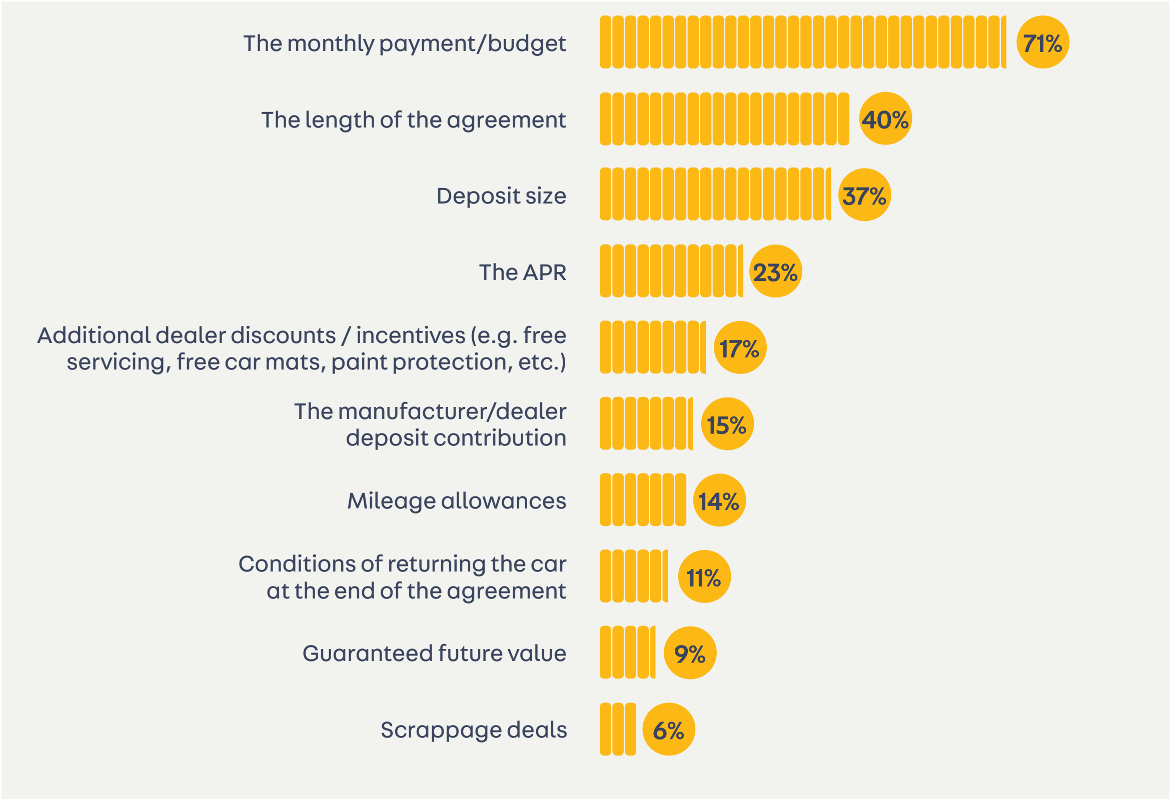
Revealingly, nearly half (48%) of all buyers that purchased in the past six months didn't plan or budget for other expenditures beyond the upfront cost of the vehicle itself. For those that did, the most common factor budgeted for was insurance, at 85%, which was the case for all age groups. This was followed by road tax (74%) and fuel costs (62%). Not surprisingly, the cost of fuel was more of an important financial consideration for younger car buyers (67%). For older and more experienced drivers (35-54 years old) who are more familiar with running costs, road tax was the most common (80%) additional

36% of those who purchased on finance did so because they couldn't afford to buy a car otherwise

Planned expenditures
(Those planning for additional costs when buying a car)



The key factors that influence a car buyers' finance choice



23% of those buying on finance identified APR as an important consideration when choosing finance

Finance isn't driving irresponsible spending, but it's clearly shaping the way consumers view the cost of a new or used car.

cost budgeted for.

This reinforces the idea that consumers are less concerned with costs outside their monthly payments. Today's car buyers' perception of cost has evolved alongside wider purchasing trends – as with mobile phones and digital streaming packages, they view price as an initial outlay and single monthly payments thereafter, not a total cost of purchase.

Finance isn't driving irresponsible spending, but it's clearly shaping the way consumers view the cost of a new or used car.

A great example of a manufacturer that recognised the opportunity within consumers' preference of a single monthly payment comes in the form of Peugeot's innovative 'Just Add Fuel' campaign – a complete finance package that simplifies the car buying and owning process.

Just Add Fuel

Mark Pickles
Marketing Director, Peugeot Motor Company

Just Add Fuel® (JAF) was born in 2010, although the work to create it began two years earlier. The insight behind the product was a simple one: many friends who bought their own car expressed envy at the simplicity of having a company car - being able to pick their ideal vehicle and know that everything else was taken care of.

That meant creating a product which included:

- PCP finance with fixed monthly payments
- Fully-comprehensive insurance
- Routine servicing
- Roadside assistance
- Road tax
- All for a single monthly payment, fixed for 3 years

As well as meaning customers simply had to "Just Add Fuel", it provided an inflation-proof deal at a time when insurance costs were soaring. In addition, with no need to shop for the best insurance rate each year, it meant less hassle – just like running a company car.

The product was an immediate success, with thousands of customers choosing to buy their next PEUGEOT on JAF, with some interesting characteristics:

- JAF customers are younger than our typical customer, wooed by the security of fixing insurance costs, and daunted by the admin of running a car for the first time
- Most of the customers are new to the PEUGEOT brand
- Around 75% stay with PEUGEOT for their next car, a great retention performance

This shift in the way we promote the product reflects its growing popularity amongst younger drivers, especially those choosing our 108 and 208 models.

The addition of a Telematics 'black box' three years ago allowed us to reduce the price of the insurance, provided the driver maintained a safe driving record. This has made the product even more popular, particularly with parents of 18-20 year olds. By giving them the peace of mind and safety of a brand-new car, with all the normal costs rolled into one simple monthly payment, plus the assurance their child is driving safely (viewed by a web portal), the product has gone from strength-to-strength.

A measure of this is that the typical PEUGEOT customer is now three years younger than it was just two years ago, bringing PEUGEOT to a group of customers who previously bought used cars.

Opportunities and risk for the industry

06

Our research revealed that for all car buyers that purchased on finance, the primary reasons for doing so were to get a better car (37%), spread the cost of monthly payments (37%) and to get a better deal (36%). The sentiment towards buying a better car was highest among younger car buyers, with 44% of 17-34 year olds identifying it as their primary reason for choosing to pay with finance.

A desire to upgrade to a better car is perhaps to be expected. As we've seen, the reason why PCP plans have become so popular is because they enable more consumers to afford higher value and higher spec cars. It's been key to reinvigorating the new car market, and will be fundamental to the growth and success of the second-hand market in 2018. However, the concept of 'better' is open to interpretation – it doesn't necessarily mean a more premium or a more expensive vehicle. When asked what 'better' meant for them, consumers gave a variety of reasons, including: **'higher spec', 'bigger car', 'newer model', 'less mileage', 'more reliable' and 'premium looking'.**

Therefore, consumers could be just as likely to end up buying a higher specification derivative or model of the same brand they were already looking at, as they are likely to switch between brands.

36%

of those who purchased on finance did so to get a better deal

Keeping it simple

The modern car buying process is already challenging and the growth of finance has made it an increasingly confusing one. The younger the buyer, the more difficulty they have in understanding their finance deal; 31% of 17-24 year olds said they struggled to understand car finance, compared to just 8% of over 55s. And those yet to buy their car find it more difficult than those that have already gone through the process; 28% compared to 16%. The fact that finance is confusing, particularly for younger and inexperienced car buyers, is not a revelation. It does however further highlight the huge opportunities available to retailers and manufacturers who can simplify the process of finance - getting finance right offers a huge opportunity for growth in the new and used car markets.

For those who went on to pay for their car outright, one in three compared different finance offers online or used an online finance calculator. Clearly, by making the process easier, there's also an opportunity to convert those willing to pay in cash to a more lucrative PCP plan.

To add some colour to our findings, we conducted a series of consumer interviews. Reassuringly, each of the car buyers we spoke to said they would prefer to organise their finance through the retailer. However, they were uncomfortable in discussing it in the dealership as they felt confused, pressured and overwhelmed. It was for these reasons they chose to organise their finance before arriving at the forecourt.

Getting finance right offers a huge opportunity for growth in the new and used car markets

An evolving model

Richard Jones
Managing Director, Black Horse

It's undeniable that change is happening and never has it been at such a rapid rate. The car buying journey is becoming increasingly digital: 80% of British motorists research online before visiting a dealership, online sales are forecast to account for a quarter of the UK new car market by 2025 and average dealer visits before purchasing are down from 4 to 1.5.

Dealers will always play an important role as there is still no substitute for the human interaction that a visit to the dealership offers. Our research shows that 45% of people want face-to-face guidance and 80% of drivers are unlikely to buy a car without test driving first. However, the dealer's role is evolving and they are now part of an integrated buying experience rather than a one-stop shop. So, what does it all mean for the future of motor finance?

So far, we have seen the digitisation of models by existing players such as ourselves, who look to focus attention on improving the customer journey and ease of use. We've also seen a handful of manufacturers introduce direct to customer propositions including point of sale finance, and we've seen some innovative models successfully simplifying the traditional car buying journey.

I believe there are three key factors which will drive the market fundamentals for 2020 and beyond:

1. How customers wish to do business with us. Customer demands will only grow, as they seek tailored solutions, via multiple entry points on their platform of choice, around the clock. The next generation of would-be car buyers are also likely to increasingly seek usership over ownership and this may bring with it the need for a new type of product entirely. Building a combined physical and digital process – bricks and clicks – will be essential to a coherent customer journey.

2. Increasing regulatory attention. The focus on affordability and rising customer indebtedness is to be welcomed, in support of the best customer outcomes. It has the potential to bring about more focused regulation of our industry and to introduce further initiatives to improve customer understanding of finance options. Dealers and finance providers take the responsibility to ensure products and pricing are explained clearly and in detail to help customers to enjoy a professional and transparent buying experience.

3. Who owns the risk. Where residual value exposure sits and how it is managed is of increasing concern for the regulators, particularly with the popularity of PCP. As exposure grows, so does the need for greater controls to be in place to prevent customer detriment or financial failures.

There is no single solution to the vast array of potential changes which lie ahead. By building flexible, clear products and by creating an innovative, future-thinking business strategy which can be delivered through a professional workforce, providers will be able to respond to whatever scenario plays out in the future.

What's next for finance

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When it comes to automotive finance, it's worth looking outside the automotive sector.

Mortgages are experiencing a digital revolution, with increasingly more brokers conducting their business online. One mortgage broker, Nuvo, is going a step further with the launch of a Facebook Messenger service, incorporating Artificial Intelligence. Accessed via Facebook's Messenger platform, the Nuvo chatbot is able to suggest the best mortgage options in under a minute. For the time-poor customer, accessing the chatbot via Facebook makes the chore of mortgage hunting simpler and easier. Eventually, Nuvo plans for the whole mortgage application process to be completed via the chatbot.

It is unlikely Nuvo will be alone for long, as many are making strides towards automating the mortgage application process. The major lenders are working hard on developing the technologies that will enable consumers to apply online and receive mortgage offers from multiple lenders, as well as looking at joining the mortgage application processes together in one automated integrated system, like Nuvo is intending.

It might be some time before the motor finance industry is able to offer the same level of innovation, but it does offer us an exciting glimpse of where the market could be heading, particularly as it strives to make the finance process more efficient, and more convenient for car buyers.

This will become of increasing importance as the market continues to face familiar headwinds from Brexit, diesel scaremongering and consumer uncertainty. Whilst these challenges will persist, for the pioneering retailers who are willing to adapt and evolve their businesses, they're far outweighed by the opportunities that lay ahead.

As we've seen, the used car market has the potential for spectacular growth, as does electric adoption. However, both will depend on the availability of finance – to be competitive, to be compelling and to be simple. Contrary to the negative commentary, the finance bubble is anything but set to burst. It's going to grow, but only if the industry and the government allow it to do so.

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Research methodology

Consumer research

Auto Trader partnered with Join the Dots, a leading consumer insight research agency, to analyse and reveal the car buying behaviours of over 4,000 UK motorists* who had either purchased a car, or were intending to do so in the next six months. Motorists were asked about their car buying and selling behaviours, including the method of purchase, in order to understand the effect finance has on purchasing power of new and used cars.

*Motorists in this instance are defined as full UK driving licence holders.

Auto Trader marketplace search data

Auto Trader extracted data from its marketplace to analyse the movements of used car prices and report on the search behaviours of UK car buyers. The data used in this Report includes specified search behaviour for fuel types and extracts from the Auto Trader Retail Price Index.

Auto Trader Retail Price Index

The Auto Trader Retail Price Index combines and analyses data from c.500,000 trade used car listings every day, as well as additional dealer forecourt and website data (OEM, fleet and leasing disposal prices, as well as pricing data from over 3,000 car dealership websites and data from major auction houses across the UK), ensuring the Index is an accurate reflection of the live retail market.

About Auto Trader

Auto Trader Group plc is the UK and Ireland's largest digital automotive marketplace. Auto Trader sits at the heart of the UK's vehicle buying process and its primary activity is to help vehicle retailers compete effectively on the marketplace in order to sell more vehicles, faster. Auto Trader listed on the London Stock Exchange in March 2015 and is now a member of the FTSE 250 Index.

The marketplace brings together the largest and most engaged consumer audience. Auto Trader has over 88% prompted brand awareness and attracts an average of 55 million cross platform visits a month, with circa 70% of visits coming through mobile devices.

The marketplace also has the largest pool of vehicle sellers (listing more than 450,000 cars each day). Over 80% of UK automotive retailers advertise on autotrader.co.uk

For more information, please visit http://trade.autotrader.co.uk

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