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Only the Fed Can Rekindle America's Love for Cars

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4–5 minutes

High prices, high interest rates and a cyberattack: Americans have had plenty of reasons to avoid car dealerships lately. It is testimony to the strength of the economy that more consumers aren't being put off.

New-vehicle sales clocked in at a seasonally adjusted annualized rate of 15.3 million in June, according to data provider Wards Intelligence. That was lower than forecasts—probably because many dealers' IT systems were hit by a hack perpetrated against software supplier CDK. A return to manual workarounds in a peak selling season cost 50,000 sales, according to an initial Wards estimate. Those sales will likely come in the second half instead, boosting July's SAAR by 0.6 million.

Vehicle sales used to be a closely watched barometer of economic health, but the signals became unreliable when pandemic lockdowns and then microchip shortages limited production. From the summer of 2021 until last year, the number of cars sold depended on what was available on dealer lots. Supply has now normalized, making sales once again a useful indicator of consumer demand.

Stepping back from the monthly gyrations caused by the cyberattack, a picture emerges of a market stuck in middle gear. SAAR hasn't moved far from the 16 million mark for over a year—a big step up from the 2020 lows but below the 17 million to 18 million considered consistent with a strong economy before the pandemic. The combination of high vehicle prices and high interest rates has likely pushed some less affluent consumers into the secondhand market.

"This may be the new reality with interest rates over 7% for new vehicles," says Jessica Caldwell, head of insights at Edmunds, the automotive-research company.

Fueled by shortages, new U.S. vehicle prices peaked at roughly $50,000 at the end of 2022, according to Cox Automotive data. As supply has normalized and interest rates have risen, they have slipped to roughly $48,400, with no end to the decline in sight. Still, that is well above prepandemic levels. Discounts to sticker prices offered by manufacturers likewise continue to creep up, but they remain modest by historical standards.

For manufacturers, the result is a gradual erosion of profit from the record levels achieved during the era of scarcity. Among the 14 non-Chinese manufacturers with a market value above $25 billion, only Kia, Ferrari and General Motors are expected to show growth in net income this year, based on FactSet consensus numbers. The U.S. market isn't the only reason, with the rise of Chinese automakers—still mostly within China itself—squeezing Tesla and the German manufacturers in particular.

The new normal is also creating new winners and losers. Toyota was the standout U.S. market-share gainer in the first half, with sales up roughly 14% year over year, it said Tuesday. The Japanese brand's promise of reliability at a reasonable price is well-suited to today's more cautious market. Its hybrid portfolio has also helped as consumers embrace alternative powertrains but hesitate to commit to the expense and charging headaches associated with fully electric vehicles.

The losers were Tesla and Stellantis, with sales down 14% and 16%, respectively. Both the EV pioneer and Stellantis's big-money spinners Jeep and RAM sit at the more expensive end of the U.S. market without being luxury brands.

While the car market has held up better than many expected in the face of the highest interest rates in a quarter-century, signs of consumer caution abound beneath the surface. Only rate cuts from the Federal Reserve seem likely to shift sales into a higher gear.

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