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# BLUE BOOK Market Report

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## MARKET ANALYSIS:

### Market Share Volatility; Japanese Losing Ground Due to Supply, Domestic and Hyundai Cleaning Up

- Alec Gutierrez, manager of vehicle valuation, Kelley Blue Book

September inventory figures for Japanese brands improved slightly over August, giving the first indication that the worst may be over. An increase of nearly 15,000 units provides a signal that in the coming months more inventory should become available. Additional product cannot arrive soon enough for dealers in the U.S. as they continue to give up share in their most important high-volume segments. Overall, Japanese market share has declined 4 points since 2010, dropping from 38.6 percent in 2010 to 34.8 percent through August of this year. This 4 point drop equates to a loss of more than 300,000 potential sales that were diverted primarily to the domestic and Korean manufacturers. Although overall Japanese share is down 4 points overall, there are more pronounced declines in a handful of crucial segments.

Share in the ultra-competitive compact car, mid-size car and compact crossover segments is down significantly for the Japanese, due to their inability to meet high demand as well as improved offerings from the competition. Additional inventory is crucial in these segments, especially for highly anticipated redesigns such as the 2012 Toyota Camry, 2012 RAV4, 2012 Honda Civic and 2012 Honda CR-V. Among all Japanese brands, Toyota and Honda have taken the most significant hit in terms of overall market share. Toyota and Honda suffered most from the earthquake, shedding 2.5 points and 1.5 points, respectively, allowing Hyundai, Chrysler and GM to each benefit by 1 point or more. While a gain or loss of a few points may seem insignificant, when we examine the impact to volume and potentially lost revenue, we begin to see the importance of market share.

## Retail Sales and Share by Segment and Region

Segment/Region	2011 YTD Sales		Overall Share	
	Volume	2010	2011 YTD	Change
<i>Compact Car</i>				
Domestic	363,251	24.9%	29.2%	4.3%
European	123,006	9.7%	9.9%	0.2%
<b>Japanese</b>	<b>567,858</b>	<b>53.4%</b>	<b>45.6%</b>	<b>-7.8%</b>
Korean	190,839	12.0%	15.3%	3.3%
<i>Compact Crossover</i>				
Domestic	422,136	41.5%	45.3%	3.8%
European	27,773	1.8%	3.0%	1.2%
<b>Japanese</b>	<b>417,688</b>	<b>51.3%</b>	<b>44.8%</b>	<b>-6.5%</b>
Korean	64,692	5.4%	6.9%	1.6%
<i>Mid-Size Car</i>				
Domestic	535,005	34.4%	37.2%	2.8%
European	5,820	0.9%	0.4%	-0.5%
<b>Japanese</b>	<b>690,268</b>	<b>53.3%</b>	<b>48.0%</b>	<b>-5.3%</b>
Korean	206,126	11.3%	14.3%	3.0%

## Revenue and Volume at Stake as Japanese Replenish Inventory

The overall loss of share by Japanese manufacturers cannot be taken lightly. The earthquake and ensuing tsunami that devastated Japan on March 11 of this year will likely impact these manufacturers for years to come. Already, the financial toll has been tremendous. In fact, we determined that Toyota and Honda have lost in excess of 350,000 potential sales combined so far this year by applying their 2010 market share by segment to 2011 sales volume actuals. This loss of potential sales has resulted from the inability of Honda and Toyota to produce and import the vehicles highly demanded by consumers today. The volume lost by Toyota and Honda equates to an approximate revenue shortfall of \$5 billion and \$3.2 billion, respectively. The revenue approximation is calculated by multiplying invoice pricing less dealer holdback and regional marketing funds to the approximate sales volume lost due to the earthquake. While the Japanese have taken a substantial hit to both sales volume and gross revenue, GM, Chrysler and Hyundai have pulled ahead as the most significant beneficiaries to Honda and Toyota's missed opportunities.

GM has proven to be the primary beneficiary of Japan's lost market share by increasing share and subsequently sales by more than 130,000 units versus 2010. This equates to an approximate increase in gross revenue of nearly \$3 billion through August 2011. Hyundai is not far behind, having picked up close to 120,000 sales and \$2.5 billion in gross revenue. Incredibly, Hyundai has been able to increase share while combating inventory shortages of its own. While not severely impacted by the earthquake, Hyundai is in the enviable position of demand outstripping supply due to the highly acclaimed redesigns they have churned out during the past two years. The all-new Elantra, Sonata, Optima, Sportage, Genesis and Tucson are but a few of the top-notch redesigns greatly benefitting the brand in today's competitive environment. Although domestic and Korean manufacturers have found success capturing market share, we can't rule out the Japanese just yet.

Japanese production should be hitting full steam right about now and we are likely to see an influx of Japanese vehicles hitting our shores in the coming months. As new product arrives, we expect Toyota and Honda to increase cash incentives relative to their current levels, but generally not to exceed \$1,000. In addition to cash incentives, there are many attractive lease deals available today in the marketplace that we expect to remain through the rest of the year. It won't be as simple as upping incentives, though. The competitive landscape is like nothing the Japanese have dealt with in recent memory. Nearly all manufacturers are producing top-quality vehicles in every segment. Even the historically Japanese-dominated compact segment has seen excellent product arrive in the form of the well-received Chevrolet Cruze, Ford Focus and Hyundai Elantra. The Japanese may be down, but they are certainly not out. With several redesigns hitting our shores this year, it may only be a matter of time before the Japanese begin to recapture some of their lost share.

### Retail Sales and Share by Manufacturer

Manufacturer	Sales Volume		Overall Share		
	2010	2011 YTD	2010	2011 YTD	Change
Toyota	1,763,595	1,073,036	15.2%	12.7%	-2.5%
Honda	1,230,463	770,262	10.6%	9.1%	-1.5%
GM	2,211,041	1,694,596	19.1%	20.0%	0.9%
Chrysler	1,093,770	892,750	9.4%	10.6%	1.1%
Hyundai Kia	894,497	772,657	7.7%	9.1%	1.4%

*Sales volume for each manufacturer include sales of all sub-brands where applicable through August 2011*

## Economic Woes Continue, What Does it Spell for 2011 SAAR?

**W**ith only one quarter to go in 2011, most economic indicators suggest that the economy is still years away from hitting a level that will support new-vehicle sales resembling anything close to the days of 16 million SAAR. Unemployment, housing, consumer confidence and GDP are only but a few of the economic indicators currently pointing to a sustained lull rather than a robust recovery. If we look back to 2005, when 16.5 million vehicles were sold, we can see the economy was on seemingly much stronger footing. Of course, we now know in retrospect that the strength in the U.S. economy in 2005 was predicated on an unsustainable housing boom fueling growth and confidence that was later discovered to be unsustainable.

The latest federal open market committee statement released by the Federal Reserve on September 21 highlights even the Fed's recognition of a likely prolonged economic slump. According to the statement, while the Fed expects "some pickup in the pace of recovery over coming quarters," they also highlight the presence of "significant downside risks...including strains in global financial markets." The Fed also pointed to continuing weakness in overall labor market conditions, giving a sense that while they expect growth, it may not be very robust growth. To combat the economic downturn the Fed has kept interest rates at historic lows and pledged to maintain rates at their current levels through at least 2013. Even with rates at historic lows, banks remain reluctant to lend and the economy has yet to improve significantly.

With the current economic outlook shaky at best, there is very little indication that the economy will return to 2005 level performance for several years to come. It isn't all bad news, though. Although many leading indicators are relatively negative, a few have at least shown signs of modest improvement or at worst, stability. With this in mind, we expect very modest improvements in vehicle sales over the next several years. We still believe 12.5 million vehicles will be sold in 2011 and given the current state of the economy and the expectation for very little growth moving forward, we do not expect to see sales significantly in excess of 13 million units in 2012. More likely, we will see sales between 12.5 to 13 million units until economic conditions improve sustainably.

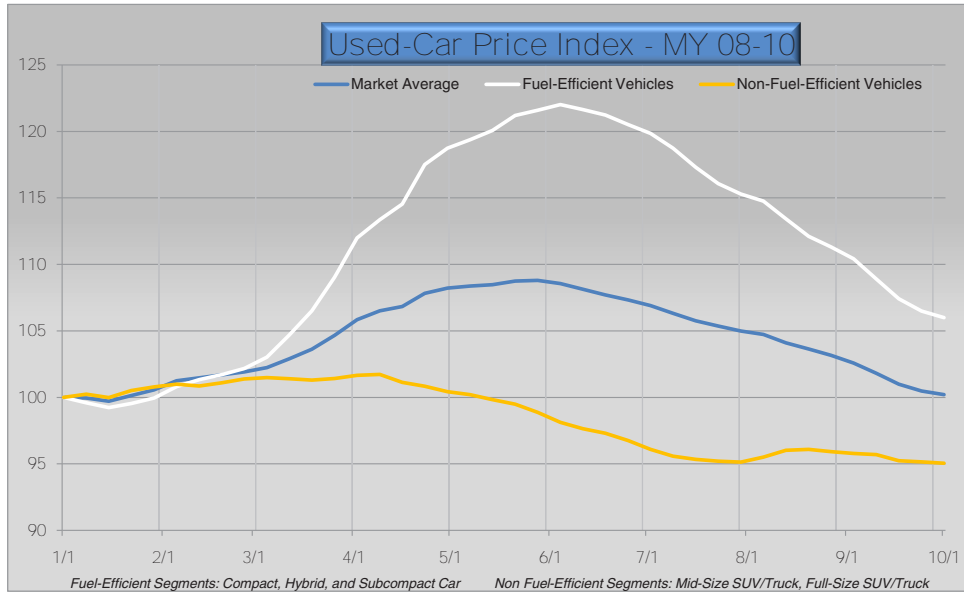
## Seasonal Declines and Fuel Price Corrections Continue

**U**sed-vehicle values dropped 2.3 percent in September, bringing the total market decline to 6.6 percent since its June peak. Compact cars have been hit especially hard since increasing 20 percent early in 2011 in response to rising fuel prices and the earthquake in Japan. Since June, values have declined 9 percent for fuel-efficient compact cars, with the most pronounced drops coming from hybrid vehicles such as the Toyota Prius, which has declined in excess of \$4,000. The fourth quarter will bring much of the same as values for compact cars continue to correct and a seasonal fourth quarter lull at auction sets in. Values are typically soft during the fourth quarter as dealer activity at auction tends to slow down during the holiday season. While the market is expected to continue to decline, Kelley Blue Book expects the drops to be relatively mild overall, likely between 1 to 2 percent per month through the fourth quarter. While overall declines should be mild, we expect compact cars to continue to correct by as much as 6 to 8 percent through year-end.

### Compacts Continue to Correct

Segment	Sep 1 - Oct 1		Jun 1 - Oct 1		YTD Change	
	\$	%	\$	%	\$	%
Hybrid Car	(\$864)	-5.6%	(\$2,521)	-14.8%	\$386	2.7%
Compact Car	(\$484)	-4.3%	(\$1,088)	-9.1%	\$1,002	10.1%
Subcompact Car	(\$272)	-2.7%	(\$1,174)	-10.6%	\$1,076	12.2%
Overall	(\$373)	-2.3%	(\$1,143)	-6.6%	(\$107)	-0.7%

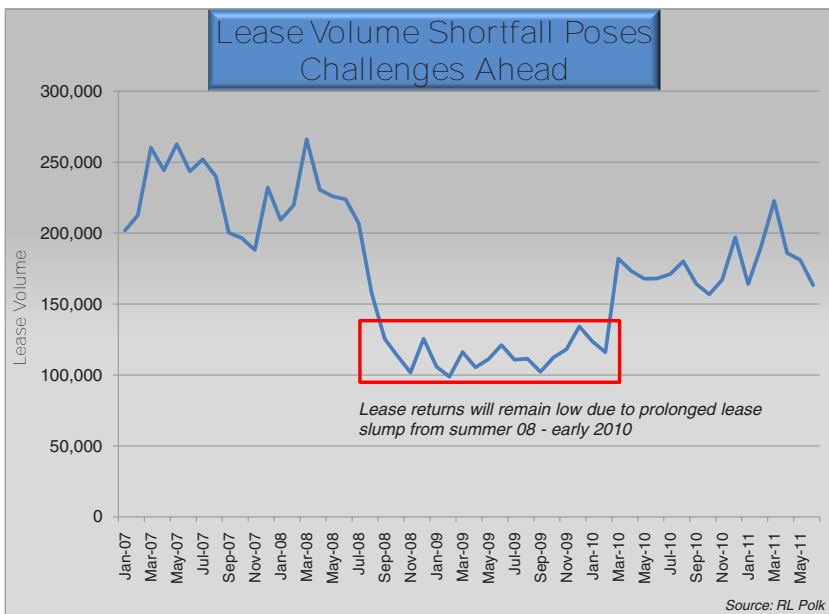
*Figures listed reflect changes to KBB Auction Value for MY08-MY10 used-vehicle values for the period listed*



### Supply at Auction to Remain Light Due to Continued Lease Return Shortfall

Although we expect values to continue to decline in the short term, a low supply of used late-model vehicles will continue to limit used-vehicle depreciation for the next several years. Used-vehicle supply at auction has taken a hit due to the drop in new-vehicle sales from 16 million units in 2007 to 10.5 million units in 2009. This steep decline in sales has led to a lack of trade-ins, fleet sales and lease returns that would typically replenish used-car supply at auction throughout the year. While already a problem for dealers, this supply shortage will likely be most pronounced for the next 6 to 12 months, due to a substantial reduction in leasing from August 2008 through March 2010.

As new-vehicle sales slipped, leasing took an especially hard hit as banks tightened up lending standards and reduced lease offers due to the uncertainty surrounding the future of both the auto industry and economy as a whole. Lease-return volume at auction has been limited for at least the last 12 months, approximately two years out from the initial decline in lease originations. Since the majority of leases cover between 24- to 36-month terms, we expect lease return volume to remain lowest through March of 2012; 24 months after leasing started to rebound. The most significant improvement will not occur until March of 2013 when three-year leases begin to return to auction. In the meantime, dealers should expect to continue to pay a premium at auction as lease returns remain few and far between.



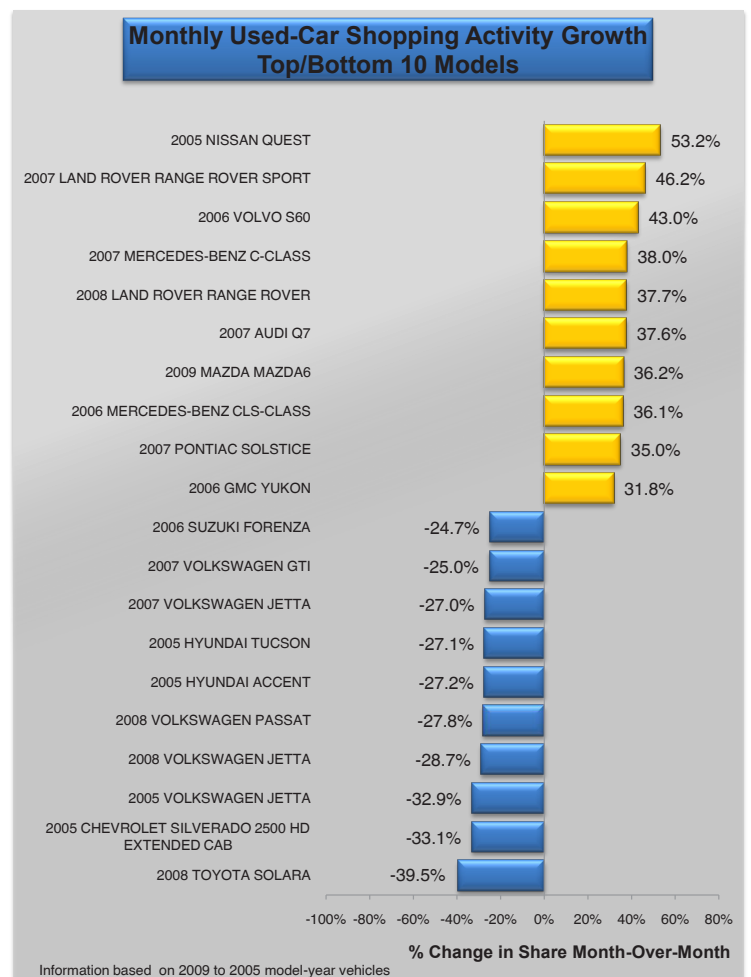
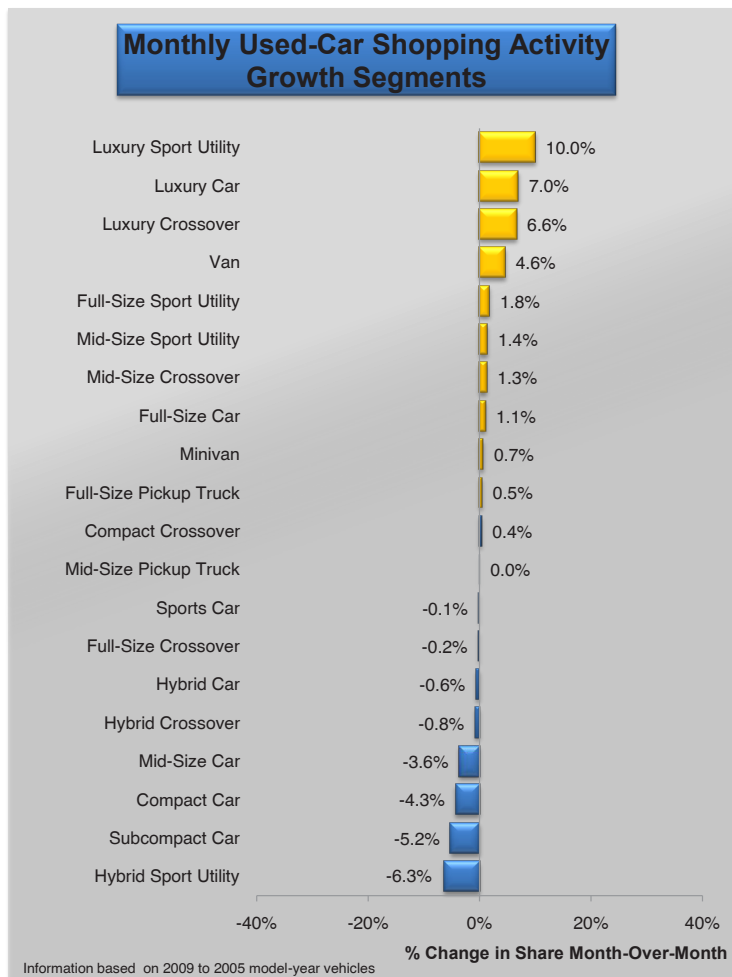
*This commentary focuses on model years 2008-2010. The statements set forth in this publication are the opinions of the authors and are subject to change without notice. This publication has been prepared for informational purposes only. Kelley Blue Book assumes no responsibility for errors or omissions.*

## Luxury Traffic Share Increases with Seasonal Demand; Land Rover Benefitting Most

Kelley Blue Book's Hot Used-Car Report captures monthly used-car shopper activity on kbb.com, including a list of the top and bottom movers in the same time period. Results are provided by the Kelley Blue Book Market Intelligence Team, in an effort to help dealers better understand which used vehicles consumers are looking at most each month.

In September, consumers on kbb.com increased their research for used-luxury vehicles, as all three luxury segments (luxury sport utility, luxury car and luxury crossover) gained in traffic share. The luxury segment drawing the most attention is sport-utility vehicles, increasing 10 percent in share month-over-month. Driving interest in this segment is the Land Rover Range Rover Sport, which jumped 46.2 percent in share from the previous months.

There are multiple reasons for the shift toward luxury and Land Rover in general. One reason for this movement is that luxury vehicles gain interest in the fall and winter months as vehicle prices decline to make room for the upcoming models years. Another reason, highly applicable to Land Rover, is that many luxury manufacturers have expanded their product portfolio and consumers are sorting through the increased vehicle options. As dealers begin planning their inventory for the upcoming fall and winter seasons, please keep in mind that there will be an increased demand for luxury vehicles.



### About Kelley Blue Book ([www.kbb.com](http://www.kbb.com))

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