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USED VEHICLE REPORT

Q4 2023 | New Cars Make Trouble for Used Cars

Executive Summary

The used vehicle market is in a transitional stage, with many of the most impactful changes coming from the recovery of the new car market. Values of nearly new vehicles are at the mercy of new vehicles, which are having a hard time making their way off the lot and are beginning to rely on discounts. The same can't be said for older used vehicles: While their values are also coming down, they're still much higher than prepandemic norms. The rebound in inventory and incentives is certainly a relief for shoppers who might consider a new car, but consumers seeking the most affordable transportation are having a harder time because the supply of older used cars is restricted.

Key Points

- **New car market recovery affects used vehicle values:** New car incentives have returned with the rebound in inventory and are helping to steer consumers back toward new vehicles, lessening demand for near new used units that were being cross-shopped against their new counterparts. This environment has made it increasingly difficult for used vehicles to retain value.

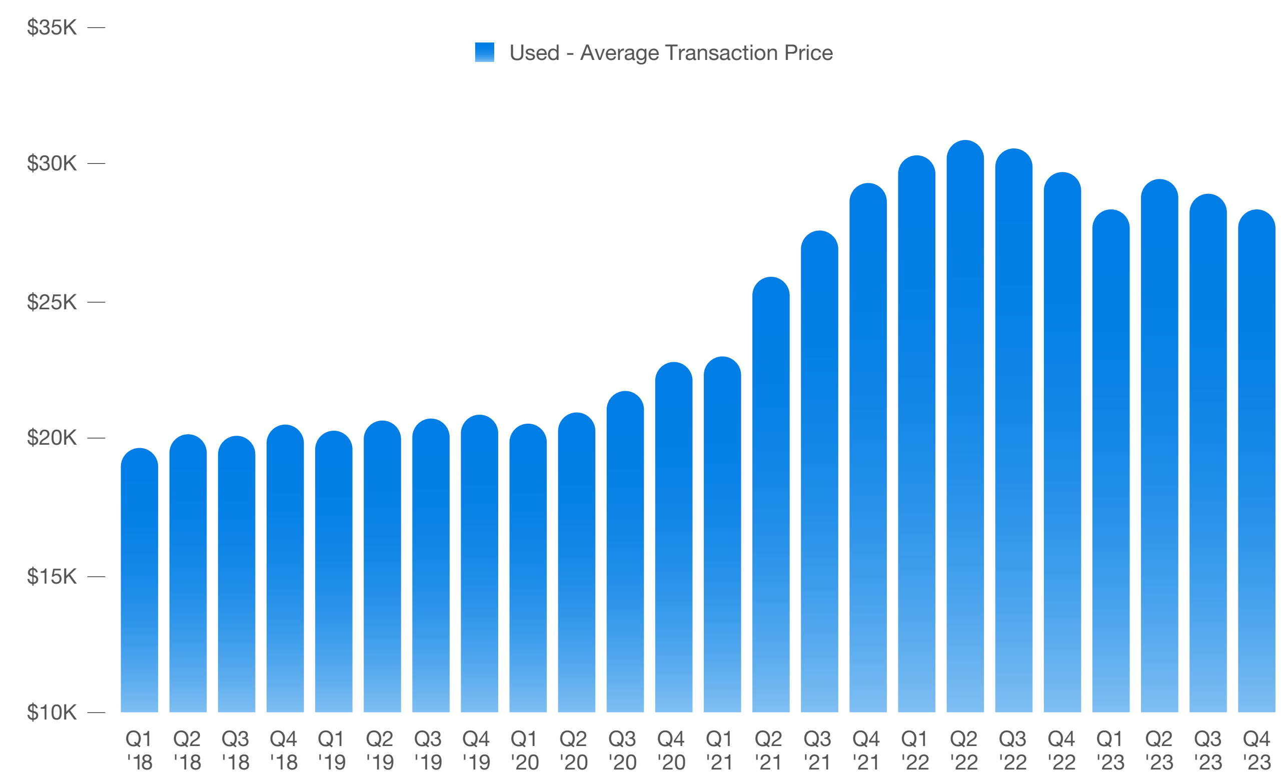
- **Trade-in values become increasingly difficult to determine:** With so many factors influencing used vehicle prices, dealers are forced to hedge their bets against value reductions, especially in cases where new vehicle counterparts are anticipated to have deeper discounts. With automaker incentive programs offered on a monthly basis and days to turn for nearly new vehicles sitting at 39 days during Q4 2023, many trade-in values will need to account for new car price fluctuations that might occur over the next month.

- **Negative equity on the rise:** While people who bought a car years ago might not see why the new car market could affect the value of the vehicle in their driveway, trade-ins with negative equity have become increasingly prevalent as used vehicle values dwindle. The vehicles most affected by negative equity tend to be newer trade-ins that were once highly sought after but now face steeper depreciation.

USED MARKET CONDITIONS

Used Car Prices Slump to a Two Year Low

QUARTERLY AVERAGE TRANSACTION PRICES FOR USED VEHICLES



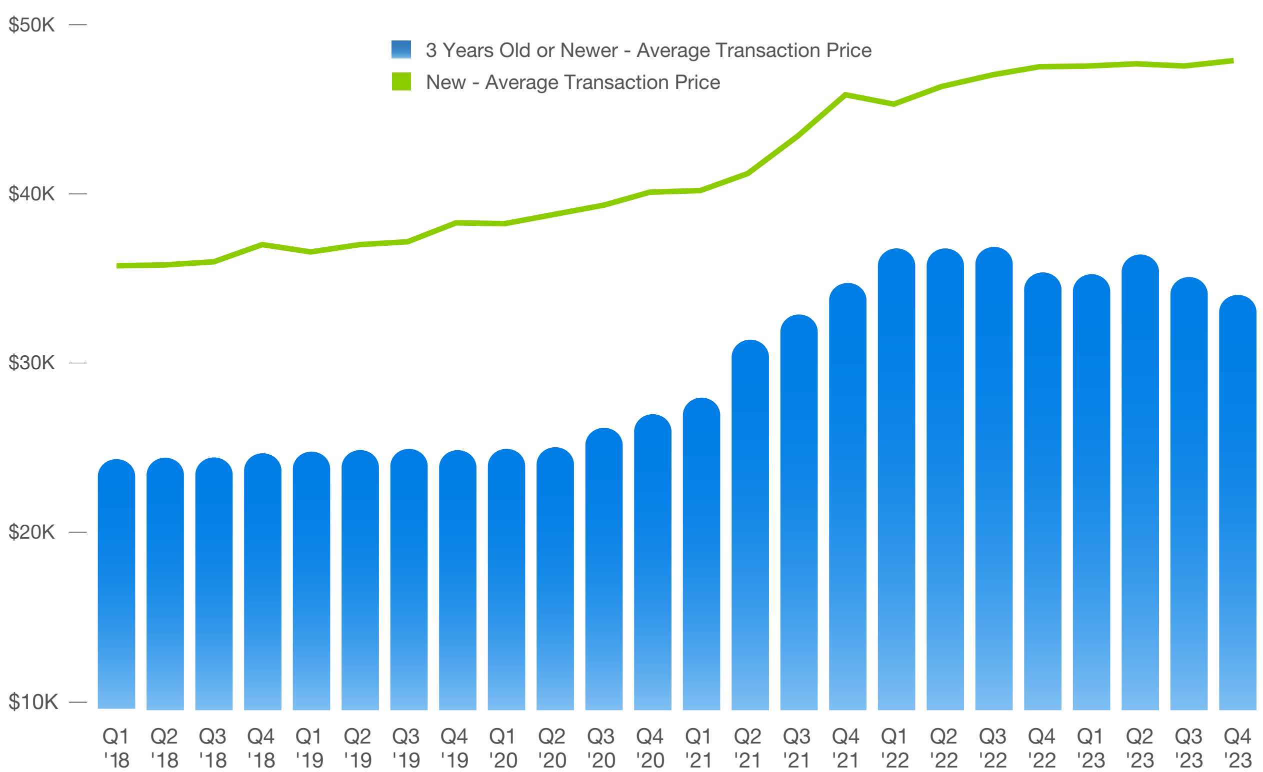
Source: Edmunds

The average transaction price (ATP) of a used vehicle in Q4 2023 dipped 4.4% to $28,371 compared to last year's Q4 value of $29,690. Even with the decrease, the Q4 2023 figure still represents a significant 38.4% increase from the ATP of $20,502 from Q4 2018. New car inventory levels are improving to the point where incentives are back and putting downward pressure on used vehicle values. Bigger is better when it comes to savings for shopping near new used vehicles versus new. In an analysis of average transaction prices of vehicles 3 years old or newer compared to ATPs for new vehicles:

- Out of all segments, luxury large cars showed the greatest savings of $48,111, with new vehicles going for $118,309 compared to used at $70,198.
- For mainstream shoppers, large SUVs are worth a look, generating an average savings of $19,966 (used vehicles going for $56,164 compared to $76,131 for new).

New Car Prices Plateau While Prices of 3-Year-Old or Newer Used Vehicles Drop

LATE MODEL YEAR PRICES VS. NEW

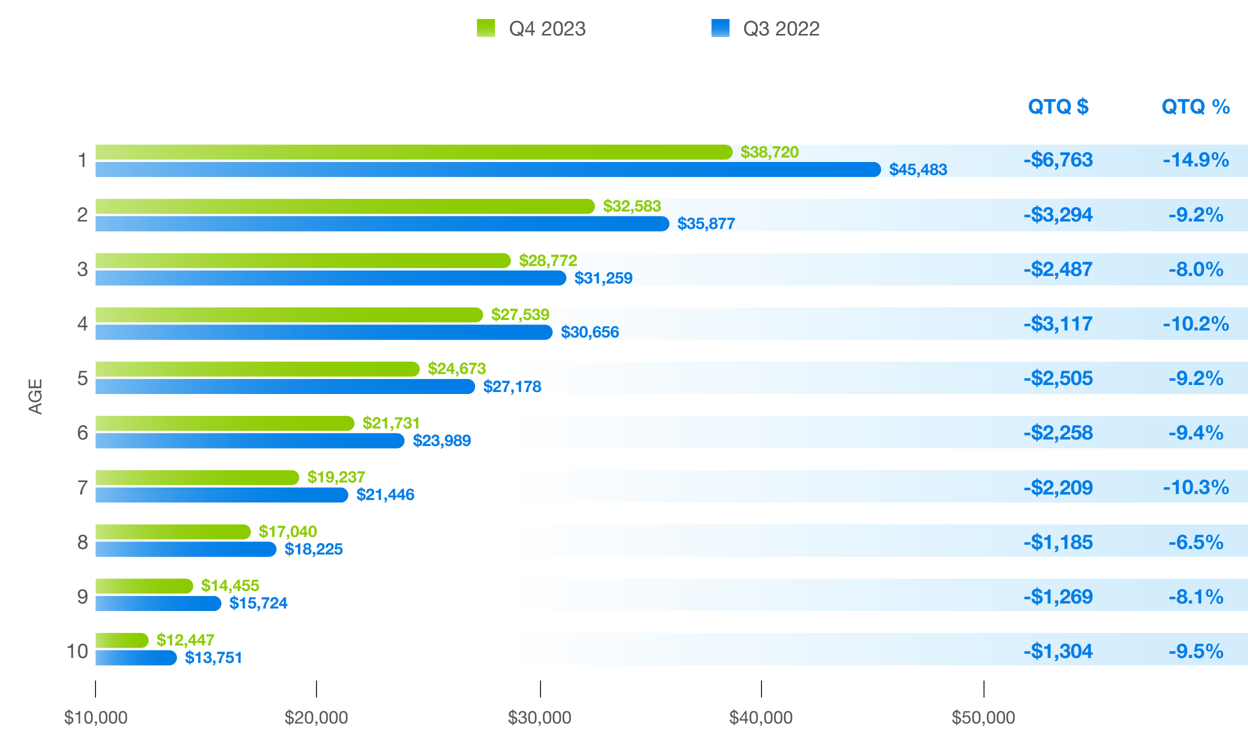


Source: Edmunds

New vehicle ATPs remain high but have plateaued considerably over the last few quarters, topping off at $48,059 during Q4 2023. The ATP for nearly used vehicles, meanwhile, fell to $34,233. Consumers on the fence between the new and used markets are no longer at the mercy of low new car inventory, but whether new car incentives are enough to offset the substantial savings within reach with a near new used vehicle remains unclear. The new versus used question gets a bit fuzzy for consumers who need a loan, as getting a subsidized low APR for a new car will be hit or miss depending on the incentives. But a low APR could tip the scales in favor of a more expensive new car as the average rate on a used car loan was 11.6% in Q4 2023 while the average new car loan rate was 7.4%.

Newer Used Vehicles Experience Considerable Price Drops

AVERAGE TRANSACTION PRICES BY USED VEHICLE AGE:
Q4 2023 VS. THE HEIGHT OF THE NEAR NEW MARKET Q3 2022

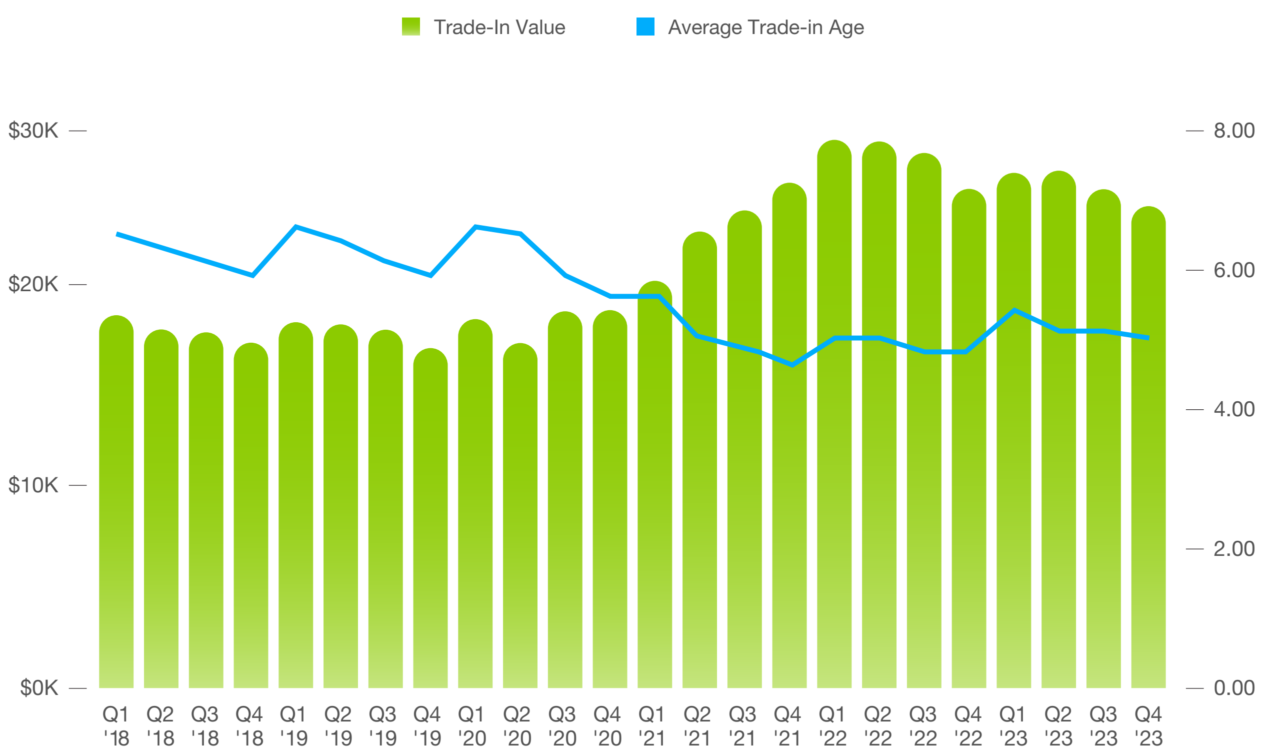


Source: Edmunds

Comparing the latest quarter against the height of values for near new used vehicles in Q3 2022 underscores how much the new car market's health affects the values of the newest used vehicles. With new car inventory more readily available, fewer shoppers are resorting to cross-shopping new versus nearly new vehicles. That, coupled with incentives on new vehicles putting downward pressure on prices, has created a considerable dropoff in the values of newer used vehicles. This combination of factors is setting the stage for a trickle-down effect on becoming more impactful to the older model year vehicles, but the lag time might be considerable given there are fewer lease returns coming back to the market versus what we have seen prepandemic and a reduced rate of rental fleet turnover.

Trade-in Values Show Dealers Hedging Their Bets

QUARTERLY AVERAGE TRADE-IN VALUES FOR USED VEHICLES

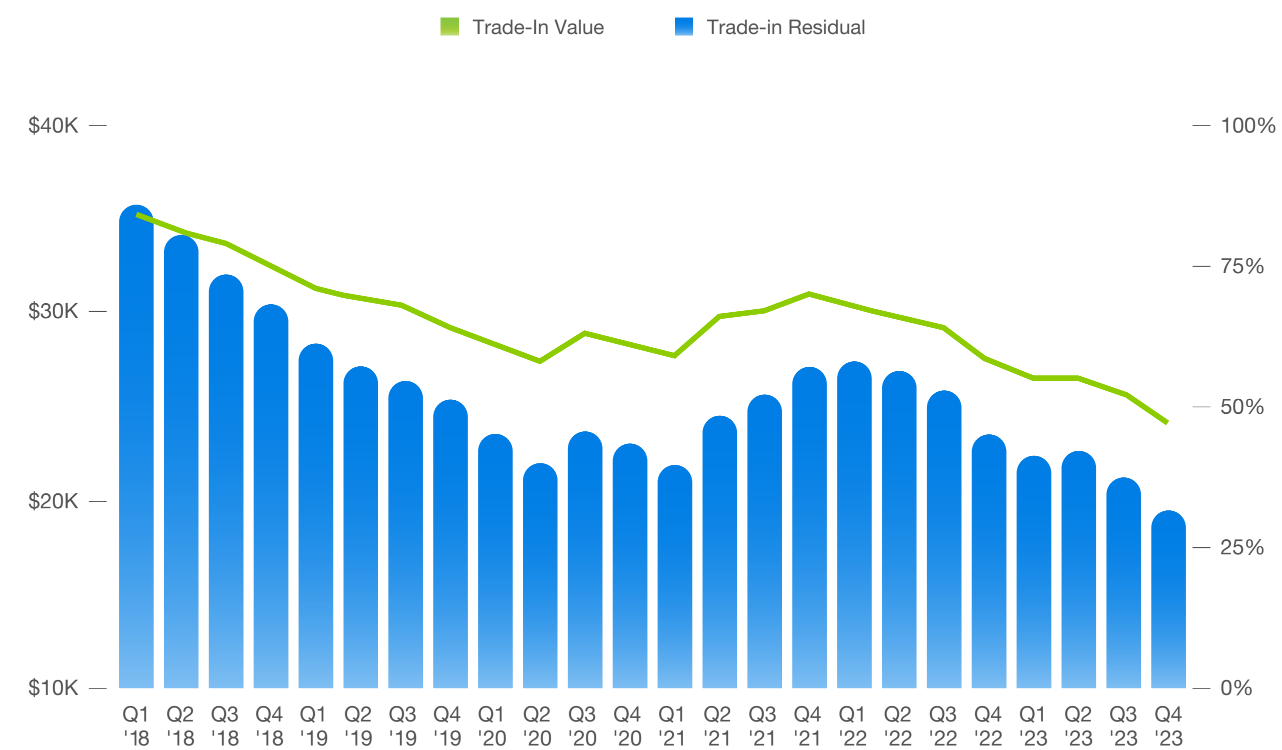


Source: Edmunds

The average trade-in value for Q4 2024 hit $25,907, which is 3.3% lower than last year's value of $26,794 but almost 40% higher than $18,516 from five years ago. One caveat is that the average trade-in age is now nearly one year younger than prepandemic — it's gone from over 6 years old to a low of 4 years old and has now stabilized near 5 years old. Although the mix of different trade-in ages affects values, overall reduced values indicate that dealers are anticipating a downward trajectory in resale values. There is also the potential for a more aggressive drop in the industry average trade-in value as we expect to see a rise in consumers with older trade-ins enter the market after sitting out the new car inventory crunch.

Trade-in Values Pick Up Where They Left Off

2018MY TRADE-IN AND RESIDUAL JOURNEY



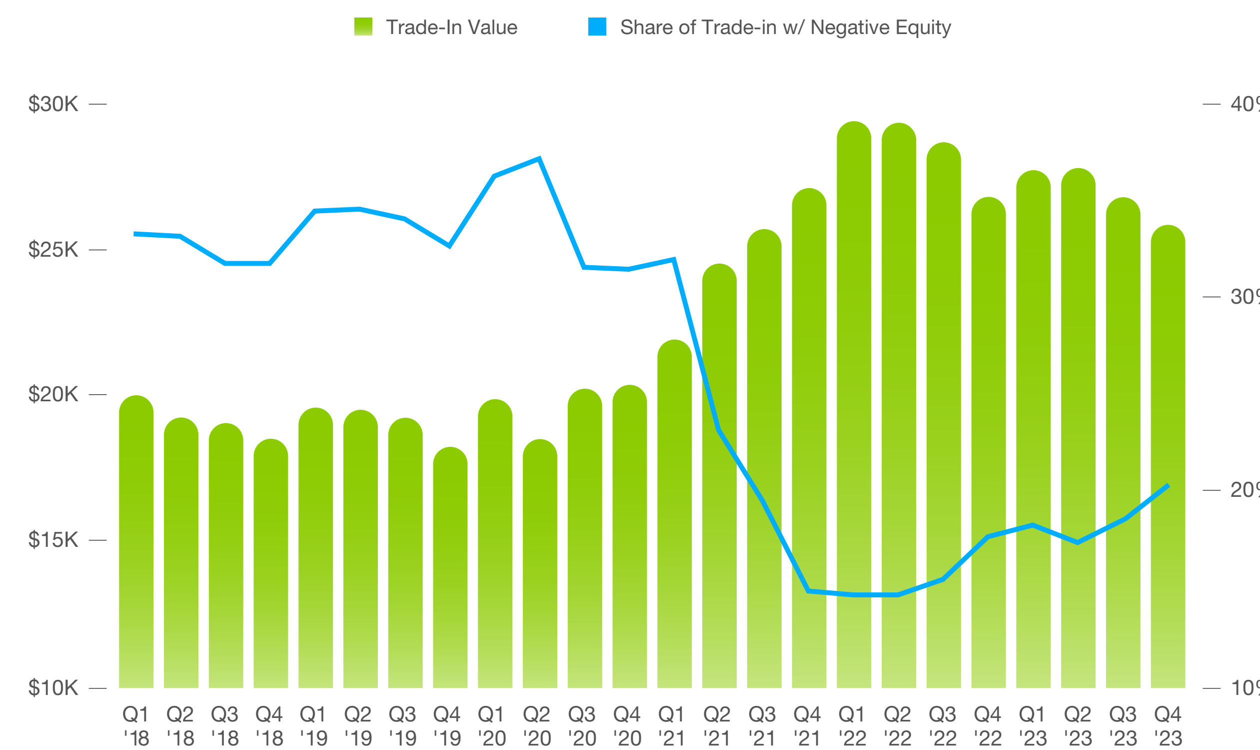
Source: Edmunds

For car owners, reality has settled back in — once appreciating vehicle values have now dipped below any previous quarter, and a typical 2018 model year trade-in is back on the typical depreciation track. For consumers with older trade-ins, the recent turn in valuations won't be felt in the same manner as for those with newer trade-ins because older trade-ins are much more likely to be closer to being fully paid off. For those with a late model year vehicle, higher ATPs and the more aggressive drop in values pose a legitimate threat as those trade-ins are further away from their equity breakeven point.

NEGATIVE EQUITY MAKING A COMEBACK

Higher Trade-in Values Don't Guarantee Equity

TRADE-IN VALUES AND SHARE OF TRADES WITH NEGATIVE EQUITY

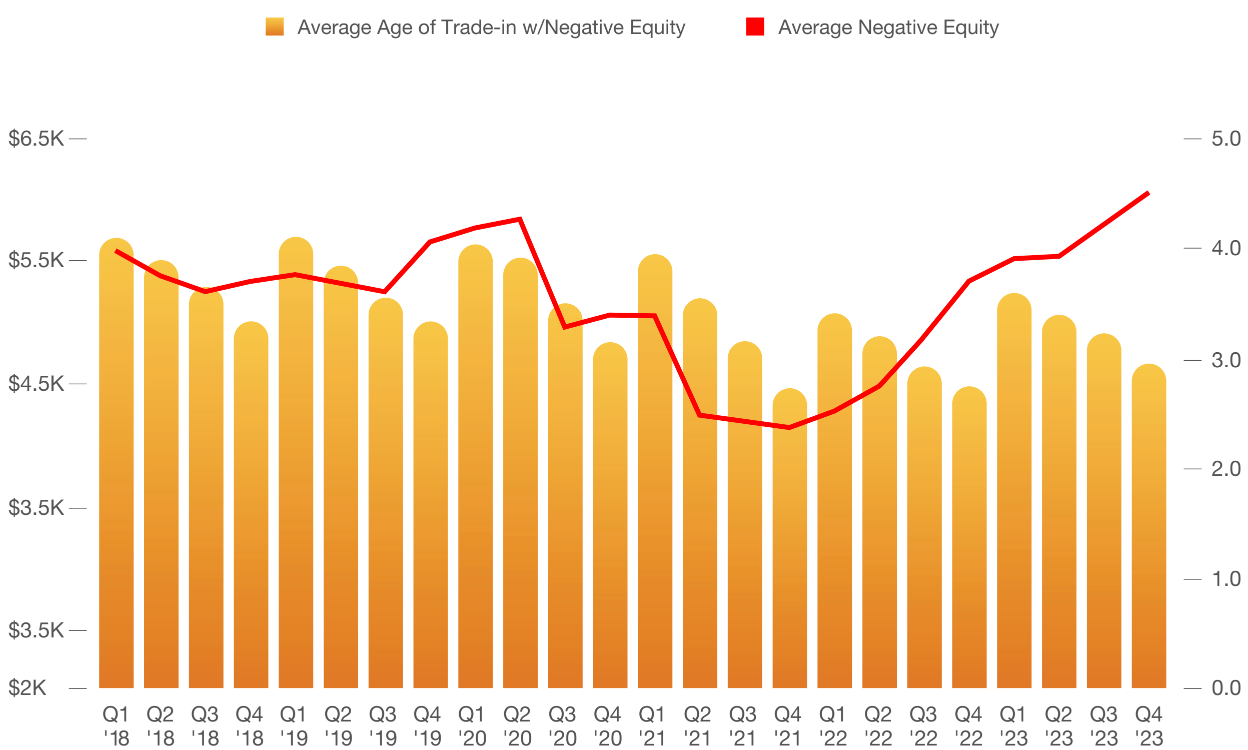


Source: Edmunds

Despite average trade-in values floating well above historical norms, the recent downturn in values has put more customers into the position of owing more on their vehicle than the trade-in value. During the absolute height of trade-in values, many consumers were shielded from having a trade-in with negative equity as dealers who were desperate for used inventory sometimes paid similar to the original purchase price.

Newer Trades Suffer From High Balances

NEGATIVE EQUITY VS. AVERAGE AGE OF TRADE-IN WITH NEGATIVE EQUITY



Source: Edmunds

Market dynamics have changed like never before in the last few years, and while some shoppers steered clear of entering an uncertain market, there appears to be a group of consumers who might be having regrets about their purchases during the pandemic. These consumers are trading in vehicles that tend to be newer and are also the ones most susceptible to reduced trade-in values due to new inventory incentives.

Looking Ahead: Used Values Normalize; Fallout Ensues

The used market will always be tied to the new vehicle market, but the correlation between the two isn't always perfectly linear and immediate. As new car incentives become more prevalent, used values will take a hit, and shoppers buying nearly near vehicles, which are cross-shopped the most against new vehicles, will be most affected. Another issue that had been sidelined for years because of high resale values has returned: consumer trade-ins with negative equity. Two more factors will exacerbate the negative equity issue: consumers who paid near or over MSRP during 2021 and 2022 have vehicle loans further from the breakeven point at trade-in, and even more recently, high interest rates on car loans increase the time before consumers pay more towards the principal and fight depreciation. As the used market begins to more readily resemble its old self, casualties are beginning to mount.

Questions?

strategicinsights@edmunds.com