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# Views on an evolving automotive industry

## Government support and incentives

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The automotive industry is unquestionably evolving at considerable pace whether through advances in connectivity and autonomy in vehicles, developments in the way that consumers access and use vehicles or changes driven by the 'electric revolution' and the industry disruption caused by the COVID-19 pandemic.

Through our series of articles, "*Views on an evolving automotive industry*", we will look at some of the legal, regulatory and compliance issues that arise from or have been magnified by these unprecedented changes.

In this third article of the series, Roddy Martin, Nanda Lau and Paul Hartley look at the tensions OEMs are facing in balancing their drive towards electrification with the immediate industry impacts resulting from the COVID-19 pandemic. In particular they look at the likely significance of increased governmental support and incentive schemes in enabling OEMs to strike such balance and the form such incentives are taking as compared against available incentives in China and those introduced following the 2008 global financial crisis.

## An industry facing an impossible balancing act?

OEMs globally have faced a perfect storm. The COVID-19 pandemic has caused financial weakness due to the heavy disruption to revenue streams, whilst the ever-tightening of emissions targets has made the need for the continued and high cost pivot to electrification increasingly time-critical.

In the short term, damage has already been done. For instance, September 2020 was the weakest September for car sales this century in the UK. Further, the expectation is that, even after the supply chain and distribution impacts of the COVID-19 pandemic ease, balance sheet pressures for OEMs will continue with global demand for light vehicles remaining subdued through 2021, with many consumers facing the economic reality that a new vehicle is a luxury they can ill-afford. At the same time, those with disposable income may be inclined to continue to look to cheaper new or used internal combustion engine (“**ICE**”) vehicles, not least whilst fuel prices are low and with the prospect of a strong used car market resulting from foreclosed finance leases.

In the medium term, however, there is no indication that the outbreak of the COVID-19 pandemic will have any dampening impact on the desire for an electric vehicle (“**EV**”) future with societal pressure to tackle climate change to deliver an environment-friendly future showing no sign of easing. If anything, such environment-focussed outlook has been strengthened through the witnessing of the environmental benefits arising from the global short term reduction in fossil fuel usage triggered by pandemic-related lockdowns.

With such societal pressure continuing to build, statutory emissions regimes globally are expected to become more and more stringent, particularly in the fully industrialised economies.

Environment-motivated targets, such as the recently announced UK policy to end the sale of new ICE cars and vans by 2030 and new hybrids by 2035, are here to stay. The US, under a Biden-led government, is likely to increase its focus in this area too. The continuation of the ‘electric revolution’ remains, therefore, a near-term inevitability, notwithstanding the long journey and significant investment required in order to sufficiently change consumer behaviour to reach the mandated targets.

As a result, OEMs and other automotive sector participants face an immediate tension between the short and medium term priorities – plugging the immediate balance sheet holes resulting from the direct economic impact of the COVID-19 pandemic or protecting R&D and capital expenditure budgets to thrive as part of the ‘electric revolution’.

### Impact on the automotive industry from the COVID-19 pandemic

- **20%** - the estimated decline in global vehicle sales during 2020
- **30.6%** - overall automotive market decline expected in the UK by the end of 2020
- **33.8%** - decline in UK car production output in 2020 compared to 2019

### The long journey to EV targets

- **2.8%** - of total vehicle sales worldwide in H1 2020 were EVs (including hybrids)
- **9%** - of (COVID-depressed) sales in Europe in the nine months up to September 2020 were BEVs or PHEVs
- **1 in 3** - UK motorists cannot currently afford even the cheapest EVs (based on a Centre for Economics and Business Research study from November 2020)

A short term focus on hybrid vehicles, particularly plug-in hybrid electric vehicles (“**PHEVs**”) may well form part of a strategy to bridge the gap (both in terms of revenues and meeting current emissions obligations) before the wholesale move to battery electric vehicles (“**BEVs**”). However, not least with the coming into force of the Euro 6d-ISC-FCM emission standard from 1 January 2021 and the greater scrutiny of PHEVs emissions, such strategy alone is unlikely to be sufficient to alleviate the current significant pressures faced by the industry.

Consequently, it is understandable that many, including western governments, have reached the conclusion that governmental support and incentives are increasingly essential to give many OEMs and other automotive market participants a fighting chance to strike the right balance of priorities (in particular to



support the associated level of restructuring of the traditional ICE production lines that is ultimately required in a pure-BEV future).

With this in mind, looking to both history and to China where the 'electric revolution' is already more advanced is helpful in assessing the form and likely success of such required support and incentives.

### The lessons from the 2008 financial crisis

Government incentives for the automotive industry were common following the 2008 global financial crisis and there is evidence that such incentives had a true benefit to the industry. For instance, a Centre of European Economic Research discussion paper from 2013 concluded that scrappage schemes across Europe in 2009 played a role in stabilising car sales and that the schemes prevented a total car sales reduction of 17.4% in countries with schemes targeted at low emission vehicles.

Notably, however, whilst there was such a positive effect in temporarily stabilising total car sales, the environmental benefits were limited, with such scrappage schemes only reducing average fuel consumption of new cars by an estimated 1.3% in countries with the targeted schemes.

Of course, a lot has changed since 2009, however, these statistics do suggest that it is not a foregone conclusion that similar incentive models from 2009 alone, if replicated, would do enough to protect OEMs as part of their medium term EV strategies, beyond freeing up

budgets as a result of a short term economic stimulus.

Given the overall public focus on the environmental agenda, new incentive schemes and support packages that do not target clear environmental benefits would seemingly be incomprehensible. Therefore automotive industry support will now need to be couched within wider sustainability or net zero carbon agendas; agendas which were not as prevalent back in 2008.

#### Examples of support packages and incentive schemes arising from the 2008 financial crisis

- **UK** - a £2.3 billion support package for the UK automotive industry was introduced, including guaranteeing up to £1 billion of loans for investment into low-carbon initiatives
- **US** - the American Recovery and Reinvestment Act 2009 provided \$6 billion to promote R&D and deployment of next generation automobile batteries, advanced biofuels, EVs and the infrastructure to support these technologies
- **France** - \$250 million was pledged by France to support car manufacturers' consumer finance divisions



## The lessons from China

China has widely been seen as leading the EV race, for instance with reports that over 1.2 million EVs were sold in China in 2019, representing nearly half of EV global sales in that year. Speaking earlier this year, VW CEO Herbert Diess stated that *"government policies are more focused on electric cars [in China] than in any other country"*. Such statements are perhaps unsurprising given China's strength in battery technology (a key component in the development and cost of EVs) which is anticipated to strengthen further not least through CATL's collaboration with Tesla through the launch of the Model 3 sedan to the Chinese market.

There are, of course, a multitude of reasons for China's overall growth and market position in respect of EVs, but the role of government incentives has undoubtedly been significant. Beijing is said to have invested an estimated \$50 billion in the industry with ambitious targets having been set by the Chinese government including for new EVs to account for 25% of car and truck sales by 2025. Beijing is also implementing the infrastructure to support this, with the long term plan of building charging points within a five kilometre radius from one another in certain areas of the city. Beijing now has over 200,000 charging points.

Further, critically China has implemented legislation which complements these incentives. For example, in the cities of Shanghai and Shenzhen, citizens have to enter a lottery or auction to be able to buy an ICE vehicle due to licencing restrictions on the

number of petrol cars sold each year. This further encourages Chinese citizens to purchase EVs rather than wait for their winning ticket, hence contributing to China's position as having the most global EV sales.

As well as this consumer-targeted legislation, this year China has issued renewed parallel measures on manufacturers with China gradually increasing the mandated EV quotas on manufacturers.

Specifically in terms of its response to the COVID-19 pandemic, the Chinese government moved quickly with the Chinese Premier announcing at a State Council meeting on 31 March 2020 that China would continue new EV subsidies for an additional two years and that government funds would be made available to compensate the replacement of diesel vehicles in key geographies including Beijing.

### Examples of Chinese incentive schemes and their impact

- **63.25%** - of Chinese consumers asked said that tax rebates and subsidies would be the biggest motivation in purchasing an EV
- China has exempt qualified EVs from 'vehicle and vessel tax' since 2012, including at one point the waiver of a 10% sales tax
- **\$1,440** - the amount some Chinese cities and provinces are offering new car buyers purchasing EVs in 2020



## China and Europe compared

At a principle level, therefore, western governments may seek to learn lessons from China as to the path forward on what incentives and complementary regulation can do for EV growth and industry strength more generally as opposed to relying purely on equivalent measures to those seen in 2008.

At a practical level, however, even if western governments were to opt to further prioritise the industry and provide the economic resources to match those provided by China, the ability for western governments to simply replicate the approach in China is not without difficulties. This is despite EV sales in Europe being reported to exceed sales in China for the first half of 2020, given such statistics are seen as being largely attributable to a COVID-19-related economic downturn impacting overall car purchases.

Consumer confidence in EVs in a number of western countries also continues to fall far short of that in China with, for instance, a J.D. Power survey from April 2020 indicating that consumer confidence in EVs in the US and Canada, particularly given range anxiety, does not correlate with OEMs' plans in the push towards increasing EV marketshare.

Further, charging infrastructure across Europe is in comparatively early development as compared to China with charging networks having to grow massively if the desired pace of the 'electric revolution' is to be supported. For instance, a study from October 2020 from the European Automobile Manufacturers' Association found that whilst EV sales had in

the last three years increased by 110%, the number of charging points had increased by just 58%, with existing infrastructure found to be unduly concentrated in the Netherlands, Germany, France and the UK.

Similarly, with respect to battery manufacturing, whilst strides are being taken such as the European Investment Bank reconfirming in May this year that it intends to provide more than €1 billion of loans to support European-based battery projects, further significant expansion of this industry in Europe is needed to deliver local supply for the level of EVs predicted by 2025 and beyond. This needed expansion will however have to navigate regulatory and consumer concerns in Europe around the wider environmental, societal and governance issues in relation to batteries and their supply chains (as identified in our previous article in this series '[Views on an evolving automotive industry: Responding to ESG-related scrutiny](#)'). This will become more prominent with the updated EU Batteries Directive aimed at ensuring that EV batteries made or imported into the EU are sustainable.

## The policies currently in play

So what have western governments done to date to support the transition to EVs following the outbreak of the COVID-19 pandemic?

In short, it is apparent that western governments and industry bodies have been keen to emphasise that their resolve to continue the 'electric revolution' has strengthened in response to societal pressures and that the COVID-19 pandemic has not slowed the necessary pace of change.

From a policy perspective, the UK government's announcement to bring forward the ban on new ICE vehicles to 2030 has arguably been the strongest example of an accelerated policy shift following the outbreak of the COVID-19 pandemic. Such desire for acceleration has, however, also been reflected through EU-wide policies in respect of (i) parts, with the European Battery Alliance having recently reaffirmed its desire to implement its Strategic Action Plan on Batteries published last year to develop a set of measures to cultivate a battery 'ecosystem' in Europe; (ii) wider EV infrastructure with, for example, EU member states having supported the CEF Transport Blending Facility program which has funded the procurement of electric, hydrogen and natural gas buses and wider EV infrastructure in Barcelona, Paris and Italy; and (iii) overall growth in EV market share, with recent reports suggesting that the European Commission is set to announce the aim of having 30 million EVs on European roads by 2030. These general policy-based measures have also been supplemented by more specific measures such as the Italian budget law for 2020 requiring public administrations when renewing their fleet to reserve a 50% quota for electric, hybrid or hydrogen vehicles and the German government having announced plans that it will require all petrol stations to also offer EV charging in the comparative near future.

However, since the outbreak of the COVID-19 pandemic, there also has been an increasing acknowledgement that policy alone will not suffice and that financial support and incentives combined with regulatory change is necessary to deliver such policy intentions.

General stimulus packages have been forthcoming with, for instance, France having introduced a €8 billion car industry rescue package with €1 billion of such stimulus going towards the encouragement of the EV transition and Germany having committed to spending €2.5 billion on battery cell production and the expansion of charging

infrastructure aiming to have one million charging stations by 2030.

Such general policies have been combined with more specific financial measures to retain and boost EV sales, including new or extended scrappage schemes and wider EV incentives and tax breaks. For instance, the French government has offered grants of up to €7,000 for the scrappage of vehicles emitting 20g CO<sub>2</sub>/km or less, which has recently been extended to June 2021 (after the initial scrappage scheme reached its 200,000 vehicle cap in just two months). In Germany, the government has offered a grant of up to €9,000 for new BEVs, re-affirming the wider support with BEVs registered between 2011 and 2030 already having a ten-year exemption from motor vehicle tax and PHEVs having a reduced tax rate. In Italy, there is a temporary extension from 1 August 2020 to 31 December 2020 for incentive premiums granted to consumers who purchase cars emitting up to 60 g CO<sub>2</sub>/km, in addition to the benefit that EVs are exempt from the annual ownership tax for a period of five years from first registration. In Spain a new scrappage programme has been announced encouraging the trade-in of ICE vehicles of a certain age for PHEVs and BEVs.

### Examples of new and extended incentives following the outbreak of the COVID-19 pandemic

- **Germany** – Extended the end date of the incentive programme for the purchase of new EVs to 2025 (originally due to end in 2021)
- **The Netherlands** – Consumers can apply for a subsidy of €4,000 for new BEVs priced between €12,000 – €45,000 and a minimum range of 120 Km
- **UK** – Since April 2020, BEVs have been exempt from road tax

From a regulatory perspective, there has been a clear acknowledgement that the EU Alternative Fuels Infrastructure Directive first implemented in 2014 needs further review, including with the European Automotive Manufacturers' Association having called in May 2020 for the European Commission to fast track its review of the directive as part of the response to the COVID-19 pandemic, for instance with a view to including binding infrastructure targets in the revised version. National governments are also expected to continue to develop their own more extensive legal frameworks in the near future.



## Conclusion

Whilst western governments should be commended for stepping up the incentive packages already seen prior to the COVID-19 pandemic and introducing new support across the industry, it is our view that even the most optimistic of observers would struggle to argue that the schemes and support announced to date will alone provide the level of funding likely to be required to address the scale of the current and future economic challenges posed in delivering the 'electric revolution' within the prevailing macro-backdrop. At best, they will act as a helpful catalyst to drive much greater levels of private sector investment; but to deliver a pure BEV future in the next 10 years or so much more is going to be needed, much sooner.

The next steps by western governments in terms of fiscal support and mandated legislation, both at a national and supranational level, may therefore prove crucial in terms of the 'global EV race' and any failure to act decisively, quickly and in a manner that protects both market participants' short term stability and medium term EV growth, may result in long-term deficiencies and insufficient pace of change in the delivery of the 'electric revolution'. Moreover, a failure to implement sufficient and effective measures will undoubtedly be scrutinised by wider society, with environmental concerns increasingly at the forefront of minds of populations (regardless of whether or not they are vehicle owners) and with this being used by policymakers to justify such expenditure on incentives and support.

For those OEMs which manage to retain sufficient flexibility in business plans and strategies whether through diversification or consolidation to react to the developing global picture, material opportunities may become available for them to thrive, where the immediate position following the COVID-19 pandemic may have otherwise looked bleak.

With all of these variables and all of the different moves industry participants and governments can make, the only real certainty is that the steps taken going into 2021 and beyond by OEMs, wider market participants and governments will likely impact the key players in, and the geographical balance of, the automotive industry for the coming decades.

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