Gem or Clunker: Success of Auto Rebate Program Debatable

By Jennifer Ginn [1]
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The economic forecast was anything but rosy when the Car Allowance Rebate System—otherwise known as Cash for Clunkers—kicked off in July 2009.

Unemployment had reached 9.4 percent. Both Chrysler and GM had filed for bankruptcy. Things were not looking good for the economy in general or automakers specifically. That’s where Cash for Clunkers came in.

For almost two months, the federal government offered car buyers a rebate of $3,500 to $4,500 to trade in an older gas-guzzler for a more fuel-efficient new car. In the end, almost 700,000 vehicles were purchased under the $3 billion program.

The success of Cash for Clunker is debatable, and determining that success depends on who you ask and what measures you use.

In the Short-Term

Mike Omotoso, senior manager of global powertrain for LMC Automotive, said Cash for Clunkers did succeed in the short-term. LMC is the industry leader in automotive forecasting.

“It boosted vehicle sales overall,” Omotoso said. “More successfully, it boosted sales of fuel-efficient vehicles and took old gas-guzzlers off the road. It did help kick-start the auto industry, which had been in a severe downturn because of the economic recession. It did give a boost to all manufacturers, specifically the domestic manufacturers, who had been struggling at that point.”

But there were many critics of the program.

Newspapers frequently cited complaints by auto dealerships that the paperwork required for the rebates was too time-consuming and took too long to be processed. A report produced by researchers at the University of Michigan Transportation Research Institute said Cash for Clunkers didn’t do much to improve the fuel efficiency of cars on American roads either. The fuel economy of vehicles purchased in July and August 2009 increased just 0.6 and 0.7 miles per gallon respectively.

Auto website Edmunds.com was a particular critic of the program, saying the vast majority of the cars sold under Cash for Clunkers would have been sold anyway. The President’s Council of Economic Advisers countered the Edmunds.com claim. A U.S. Department of Transportation survey showed that the car purchases would have taken place in closer to three years, rather than just being pulled forward a few months.
“A plausible interpretation of the available data, in fact, is that many of the CARS sales were to the kinds of thrifty people who can afford to buy a new car but normally wait until the old one is thoroughly worn out. Stimulating spending by such people is very nearly the best possible countercyclical fiscal policy in an economy suffering from temporarily low aggregate demand,” wrote Christina Romer and Christopher Carroll. Romer was chair and Carroll was a senior economist at the council at the time.

In the Long-Term

Omotoso said in the long-term, the American auto industry was going to survive, with or without Cash for Clunkers. The multibillion-dollar bailout from the federal government helped ensure that.

In the 2011 fiscal year, GM’s profits were up 11 percent, from $7 billion in 2010 to $8.3 billion in 2011. Chrysler posted its first profitable year since 2005. It made a profit of $183 million in 2011, compared to a loss of $652 million in 2010.

“It was going to head there anyway,” Omotoso said. “I would say the CARS program just sped up the process by six to 12 months, let’s say. The turnaround in the economy would have caused car sales and production to increase anyway. High gas prices were really forcing consumers to look for more fuel-efficient cars.”

The economic picture, however, was about more than just GM and Chrysler. Cash for Clunkers did have an effect on the thousands of jobs that support the auto industry, Omotoso said.

“There was definitely an effect downstream,” he said. “The tier one and tier two suppliers, people who make engines, who make steel, robots, the transportation industry, the trains and trucks that transport the vehicles and parts to the carmakers, they all needed help to survive. One of the reasons of the bailout in the first place wasn’t just to save Chrysler and GM. It was to save thousands of suppliers.”

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