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AUTOMOTIVE

Insights

AUTOMOTIVE COMPETENCE CENTER CLIENT MAGAZINE

Issue 01.2014

NEW! NOW AVAILABLE FOR ANDROID, TOO

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LUCA DE MEO

The Audi board member unveils his thoughts about future sales

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BRIC

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Promising but individual markets

SPECIAL SUBJECT

THE AUTOMOTIVE YEAR 2014

There's a lot to do! We take a closer look at the opportunities and challenges for our industry

Editorial

Ralf Kalmbach
Head of Automotive and Member of the Global Executive Committee, Roland Berger Strategy Consultants

Dear Reader,

Welcome to 2014! Before a hopefully thrilling new automotive year is gathering pace, it's time to summarize the highlights of 2013 as well as to take an outlook at the most important trends in this new Automotive Insights magazine.

Among others we focus on the prospective emerging markets. Our experts analyzed chances and challenges for the car industry in India as well as the retail business in China. As usual, every story combines our expert knowledge with hands-on advices. For instance, the article about the fleet business in the BRIC states contains nine key to-dos for western OEMs, to thrive in the growing but complex fleet business of these prospering countries.

In particular, I would like to mention the report "Know your customer – build better cars". It explains in detail, why marketing has to assume a leadership role in the product development from the very beginning. In our opinion, that is one of the important doctrines for the vehicle industry of the future.

The future is one of the topics in our interview with Luca de Meo, too: We spoke with the board member of Audi about coming sales and marketing strategies as well as role models. Last but not least we asked our own automotive experts here at Roland Berger about their personal review and expectations for the next years.

Finally, I recommend you the eMag version of this magazine that contains a bunch of extra content. Please call or write my colleagues or myself, if you have any questions or want to share your view on one of the topics. I look forward to your feedback. Until then, I wish you insightful reading!

Kind regards and a happy, successful new year,

Ralf Kalmbach

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CHINA

HOW TO SUCCEED IN CHINA

High demand for smart strategies: The retail business in China is becoming more complex with rising demands all around

The automotive industry in China is facing increasing customer demands and fiercer competition: Retail innovation can help players to prevail in the world's biggest vehicle market

The Chinese market for passenger cars and light commercial vehicles is expected to grow from 13.6 million units in 2012 to more than 19 million in 2015. These figures are based on a current study by the research company IHS. But growth will slow compared to previous years. Looking at the figures in more detail, it becomes apparent that especially the luxury vehicle as well as the lower-cost car segments are outperforming total market growth rates. Annual growth rates of approximately 14% are expected in the luxury vehicle segment, whereas the low-cost car segment makes up 30% of the market and is showing an upward trend.

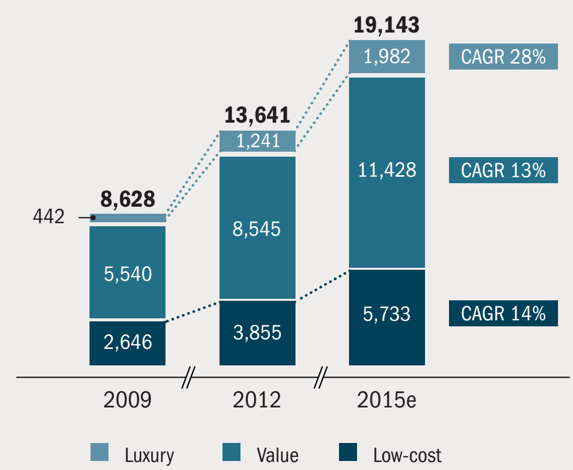
Changing market conditions

This growth potential is reflected in the market as all major OEMs are increasingly investing in these two segments. Within the luxury segment, new localized products are being introduced; the Audi Q3 or BMW X1, for example. Moreover, with luxury penetration of only around 7% – a level significantly lower than in international markets (12% in the US, 30% in Germany) – there is still much room for growth.

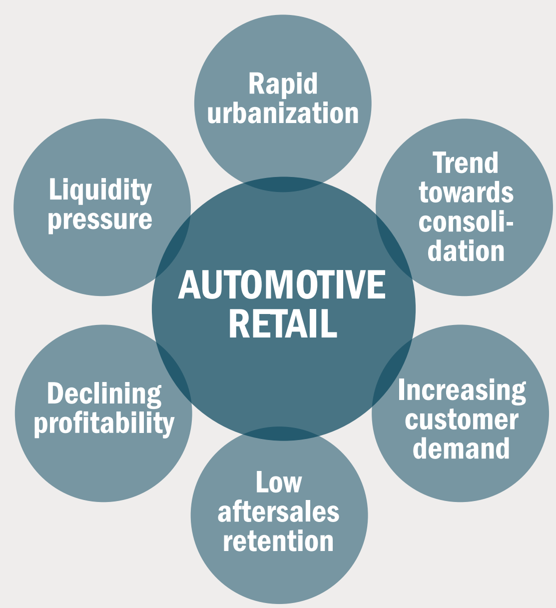
In the low-cost segment on the other hand, newly launched joint venture brands such as Baojun are expected to sell more than 150,000 units by 2015. But it's not only domestic players who have an eye on the lower end of the market. International OEMs, such as GM with the Chevrolet Sail or Volkswagen with a yet undisclosed vehicle, have announced that they will be entering this segment in the upcoming years as well. Today, the segment is dominated by Great Wall and BYD, among various other Chinese brands such SGM-Wuling, which sells more than 1.5 million cars annually.

THE LUXURY AND LOW-COST SEGMENTS ARE EXPERIENCING ABOVE AVERAGE GROWTH RATES IN THE TOUGHENING CHINESE AUTOMOTIVE RETAIL MARKET

CAR SALES IN THE CHINESE AUTOMOTIVE MARKET 1)



TOUGHENING ENVIRONMENT IN THE RETAIL BUSINESS



1) Passenger vehicles (PV) and light commercial vehicles (LCV), units ['000]

Source: IHS, Roland Berger

As a consequence, competition within these segments is heating up. To compound matters even further, additional factors such as increasing customer requirements, greater discounts and higher real estate prices are putting pressure on retail margins and are shaking up the automotive retail environment *(see our infographics at the page before)*.

Changing customer requirements in the Chinese market

At the same time, customer requirements are quickly changing. With the shift from a sellers' to a buyers' market, new vehicle options have become available. Moreover, with the extremely diverse automotive consumer landscape in China, OEMs and dealers are facing huge challenges on how to best serve their customers' needs – according to their regional preferences.

Budget-oriented car buyers, who mainly come from lower-tier cities, prefer quick and easy purchases, which is apparent by the significantly lower number of test drives compared to other segments. Nevertheless, as these buyers are fairly inexperienced, the decision to buy a vehicle is a big one. In the future, we expect that these customers will seek a more professional sales process; one that takes the whole family experience into consideration and includes extensive sales advice.

In the luxury segment on the other hand, consumers expect a retail experience very similar to luxury retailers such as Louis Vuitton or Apple. Exclusivity and entertainment offerings such as virtual interaction or an accompanying "kids land", to keep the little ones happy, are greatly appreciated and are must-haves going forward *(get further insights in the matrix below).*

Although there are significant differences in the consumer profiles of the low-cost and luxury segments, increasing sophistication and the demand for excellent service means the two segments are converging.

Given that the car is a highly emotional product and that Chinese consumers are becoming more experienced

THE LOW-COST AND LUXURY CHINESE CONSUMERS DIFFER SIGNIFICANTLY IN THEIR PROFILES, BUT BOTH SHOW AN INCREASING SOPHISTICATION

Criteria	BUDGET SEGMENT	PREMIUM SEGMENT
1 Living environment	Third, fourth or higher tier cities	First or second tier cities
2 Product experience	Mostly first time buyers with no purchasing experience and thus only limited knowledge	Partly repeated customers who already possess a certain expectation towards their vehicle, still high percentage of inexperienced buyers
3 Brand loyalty	Low brand loyalty due to inexperience	Comparatively more loyal than the budget segment but still willing to switch brands
4 Information sources considered	High importance of word-of-mouth advertising and internet	High importance of Word-of-Mouth advertising, increasing importance of internet and auto shows, multiple touchpoints with brand
5 Expectation in terms of service offering	Mainly car sales, barely demand for additional services such as aftersales service	Full service offer expected including car sales, aftersales service, financing etc.
	NEED FOR: Local sales advice & excellent service	**NEED FOR:** Exclusivity & high class customized service

Source: Roland Berger

Jammed roads ahead: The increasing number of vehicles in China means more sales opportunities for OEMs, but as well a fiercer competition

in the purchasing process, the "customer experience" is becoming increasingly important. As a result, OEMs in both market segments must find a different yet innovative approach for tackling these challenges.

Evolving retail formats and challenges for the luxury and low-cost segments

As mentioned earlier, dealers are struggling with both a more competitive environment as well as more sophisticated customers. The need to enhance the customer experience and ensure profitability represents segment-specific challenges and calls for developing new retail formats.

Low-cost car segment – finding the right balance

The major challenge in this segment is to create a relevant but yet sufficient customer experience, while overcoming the specific economics: More brands are competing in a highly crowded marketplace for a largely disloyal consumer. This makes the retail experience all the more important.

Even though dealers in the low-cost segment do not require prime locations as is the case with their luxury counterparts, they still cannot afford to be located in remote areas either. To be profitable, the location needs to generate enough showroom traffic to reach the required sales efficiency levels.

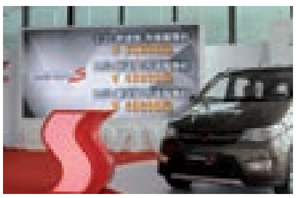
Consumers also expect a certain degree of professional sales and service advice. It is up to the management to set up a lean structure but still offer an appropriate level of professionalism throughout the sales process. It is therefore a constant challenge to find the right balance between controlling costs and enhancing the consumer experience.

Even though the 4S retail model (workplace organization method popular in Asia, which stands for "Sales, Service, Spare parts and Surveys") does provide a more enhanced customer experience, it is difficult to sustain this retail format in the low-cost car segment. In order to operate more cost effectively, structures and processes at retail outlets need to be downsized. To do so, common approaches include using satellites and sales agents as well as scaling back presales activities. The dealer network needs to be mapped out strategically according to customers' geographic requirements and

BEST PRACTICES OF INNOVATIVE RETAIL FORMATS IN BOTH SEGMENTS IN THE CHINESE AUTOMOTIVE MARKET

BUDGET SEGMENT

SGM Wuling



Cooperation with local dealers to meet local customer needs

High share of sales agents working closely with local dealers to ensure a deep understanding of the rural consumers

Great Wall

Best-in-class budget car sales processes

Lean organization to meet economics of the budget segment

Regional dealers to speed up the expansion process

Upgrade to 4S Model to enhance the service offering

PREMIUM SEGMENT

Audi City Beijing

Digital showroom allowing the consumers to configure their cars with multi-touch screens and 3D projection technology

Material lab to experience the car first-hand

Private customer lounge to enhance the exclusivity

Land Rover Experience

Off-road test drive to experience the product first-hand under extreme conditions

Driver training sessions to educate consumer and convince of functional attributes

Corporate team building events to deliver extraordinary experience

Source: Roland Berger

depending on the city/location. Great Wall, for instance, differentiates its sales network even from model to model in order to minimize its investments and tailor its efforts to its product offering.

Chinese consumers rely heavily on word-of-mouth so that dealers need to be "localized" within their region in order to guarantee an approach suitable to local customers. Independent sales agents, who can offer a cost-effective approach and at the same time have relevant local market knowledge, are becoming increasingly popular. These sales agents make it possible for dealers to reach neighboring cities faster and at lower cost.

Luxury car segment – from wholesale to consumer-centric

In this segment, dealerships are facing very different challenges. Chinese consumers are especially demanding in terms of VIP treatment and expect luxury brands to offer them exclusivity, thereby reinforcing their status in society. This means that brands in the luxury segment need to go to great lengths to create an extraordinary experience using new retail formats and retail-related events.

New formats, such as sales-only stores in premium inner-city locations, temporary formats at event and exhibition centers and customer experience centers have emerged in China, aiming to enhance brand communication and customer premium experience. By giving the consumer the opportunity to experience the product firsthand through test drives and other realities, the brands aim to evoke associated emotions.

Since these brand centers are usually operated by the OEMs themselves, a clearly defined transfer system to the surrounding dealers needs to be ensured. Consequently, the interaction between these new retail formats and traditional dealers requires more sophisticated coordination processes and clearly defined roles and responsibilities. The multiple channel and store formats complicate network planning and require a thorough analysis of the target locations and the customer structure. A further increase in format variety such as service pickup or drop-off stations at airports is expected, as aftersales services are becoming increasingly important.

Yet another challenge for luxury brands is how to personalize the individual experience and tailor it to target customers and the brand's DNA. This means luxury brands must be consistent with the underlying motivations as well as the needs and aspirations of their target group. This makes it essential to capture customer information using CRM systems, profiling and online data.

As the number of vehicle models rises, sales force differentiation is required to manage the competencies, knowledge and experience necessary for the respective sales processes. In this regard, luxury retailers often lack qualified staff as rapid expansion means proper training of the sales force was frequently neglected. OEMs must therefore enhance their training programs for sales managers. Given the fact that Chinese consumers take various information sources into consideration, luxury brands must offer a seamless consumer journey.

Best-practice examples

Several best-practice examples in both segments of the Chinese automotive industry have been identified to overcome these challenges. In the low-cost segment, SGM Wuling and Great Wall focus on regional dealers and independent sales agents, allowing them to expand quickly at limited cost. This approach ensures proximity to the local markets and a deep understanding of the regional consumers. Carmakers can thus manage to keep their sales organization lean and yet tailor it to the customer.

In contrast, in the luxury segment Audi City offers its consumers an extraordinary digital experience with its car configurator, which displays the customized vehicle on life-size 3D screens in a prime downtown location in Beijing. Another best-practice example is Land Rover, which focuses on event character and provides offroad test drives to experience the car firsthand under extreme conditions. BMW recently opened a Brand Experience Center in the heart of Shanghai, located at the former exposition center *(see infographic on the page before)*.

Carmakers should consider best practices from other industries such as fashion or grocery retail, which excel in integrating digital sales enhancements. As China has a smart phone penetration rate of 66%, new technologies such as QR codes or push marketing via social media will have a major impact on automotive retail innovation. Tesco, for instance, is experimenting in Asian countries with images of actual supermarket shelves in subways, allowing consumers to directly purchase products by scanning in the corresponding QR codes. This method could translate into an interactive and intuitive sales process in the low-cost car segment, reducing the number of staff needed in dealer outlets.

And fashion e-tailer Mogujie provides us with a best-practice example too. It successfully leverages the trend toward micro-blogs and the Chinese preference for word-of-mouth advertising. Mogujie created a platform for its consumers and allows young women to become experts and advise other consumers. This means the voice of the local consumer becomes the brand's strongest ambassador. As luxury cars embody considerable passion, this segment could promote its products quite cost-effectively by giving their community a voice and platform.

Even though automotive retail business in China is becoming more complex with rising demands all around, new technologies and new consumer touch points enable automotive brands to meet these challenges.

The key challenge, however, will be to integrate new technologies and formats into current structures and create a consistent and segment-specific customer experience.

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"WE HAVE TO THINK OF THE CAR AS BIGGER THAN THE CAR"

Luca de Meo, board member at Audi AG, speaks about future vehicles and appropriate sales and marketing strategies of tomorrow

INSIGHTS In your view, what are the three biggest challenges facing automotive sales and marketing over the next five years?

LUCA DE MEO In our industry we are used to looking even further ahead. Because when we develop a new automobile today, we bear in mind how the needs and preferences of our customers are going to evolve over the next ten or fifteen years. Our world will have become dramatically more digitized and connected by then, and that offers huge opportunities for sales and marketing.

What does that mean specifically?

Already today, we are seeing the channels that we use to get in touch with our fans multiply at an exponential rate. Our ambition is to offer people a consistent, thrilling brand experience wherever and whenever they come into contact with Audi, whether that is in real life or in the digital world. The same applies to the progressive internationalization of our business. Because more and more people are fascinated by the dream of driving a premium automobile – increasingly so in markets that were not really on our map until just a few years ago. Our goal is to provide an authentic Audi experience for all of them, all around the globe.

How important are your dealers in that regard?

Very important! We will only be able to achieve that goal in close cooperation with our dealer partners. Our dealers are independent entrepreneurs and approach their business in a thoroughly entrepreneurial way. They are committed to Audi because they are convinced by our products, our brand and our joint success. It is one of our top priorities to make sure that remains the case in the future. To put it another way, we want to offer them the most attractive franchise in our industry.

What can the automotive industry learn in terms of sales and marketing from Apple, Amazon and Tesco?

Every industry operates according to its own rules, and compared with the ones you have mentioned I think the automotive industry deals with one of the most complex and technologically sophisticated products. But we all share the same ambition: We want to make life easier and better for people. That is the fundamental motivation that has been driving the evolution of the car for more than a century. We will be able to play our part even more effectively if we see our task as involving an overall system that goes beyond the core product.

What plans do you have in mind?

Connecting the car comprehensively with its driver, other road users and the infrastructure, and letting them all speak the same language. We will then have put genuine mobile devices on the road and enabled them to develop an astonishing level of swarm intelligence by sharing the same data flow. An incredible advantage for drivers. I always tell my team that we have to think of the car as bigger than the car. Obviously, we are also looking at exciting examples from other industries that have trodden a similar path with their products.

How will you and your team generate "Vorsprung" in marketing and sales?

"Vorsprung durch Technik" is Audi's brand DNA. It first and foremost describes our technological ambition, but also goes much further: it is the attitude that characterizes the entire Audi team and pervades everything we do, across every area of our company. Because we want to be the most progressive premium brand in the automotive industry. Therefore, we need to get very close to the customer every day, be present in their dreams and visions, but also in their very practical requirements and concerns. And we need to keep reflecting continuously on whether we are doing the right things. We often find that we need to depart from the familiar, easy path and instead choose a course that is arduous, but far more exciting. We have defined three very simple but effective control questions that we ask ourselves for every project: Will it make us better than our competitors – better at meeting our customers' needs? Will we be faster to market and be able to offer our customers genuine innovations? And will we be able to scale up our ideas and roll them out internationally? Because big ideas fly over borders – I am absolutely convinced of that. If the answer is yes to all of these questions then we see the respective project as a pure Audi thing.

What role will the car dealer play in the future?

For our customers, the dealer is the face of the Audi brand and that will remain so in the future. For most people, a car is the second-biggest investment they ever make, assuming they also buy a house. They obviously do a lot of research on the Internet, on social networks and through digital dialog with us as a brand. But when it comes to their final decision on whether to buy, the face-to-face conversation with the dealer still counts for much – it is about a relationship of trust between me and my Audi dealer. That is particularly so in the premium segment, where I have millions of different equipment options and technologically very sophisticated assistance systems to choose from in order to customize my very own personal Audi to my needs, like a tailor-made suit.

Will we see Audi direct sales to end customers over the Internet?

No, but digital technology will make the shopping experience better for our customers. What matters to us is offering a seamless, universal brand experience encompassing the real world and countless different digital channels. That is why we are also supporting our dealers with a large number of tools that enable them to present themselves professionally on the web. We see the Internet as the biggest showroom in the world, and our dealers as the competence center on the ground close to the people. We want our customers to be able to switch as freely, quickly and effortlessly as possible between the various different options for coming into contact with Audi.

What about the "Audi City" concept in this regard?

Audi City shares the same philosophy: a relatively small boutique in top downtown locations in major international cities. It does not need to have a single physical automobile but nevertheless provides the experience of the entire Audi portfolio, including all customization options, through life-size digital animations. We have already opened two such cyberstores in London and Beijing, with the third location set to open in Berlin at the start of next year.

■

Luca de Meo (46) is member of the board at Audi AG and responsible for marketing and sales. The Italian-born manager studied marketing in Milan. After management jobs at Renault, Toyota and the Fiat Group, de Meo joined Volkswagen in 2009 as Head of Marketing for the VW brand. In September 2012 de Meo became board member at Audi.

The Audi Group comprises the brands Audi, Lamborghini, Ducati (motorcycles) and Italdesign Giugiaro. It is among the world's leading premium carmakers. The core brand Audi sold 1.45 million vehicles in 2012, almost 12 percent more than in 2011. Driven by these sales figures, the group's revenue rose by 10.6 percent to EUR 48.8 billion. The operating profit was EUR 5.4 billion.

Right of way for economic growth: The automotive industry is a major contributor to the national GDP

DRIVING ECONOMIC GROWTH

The impressive contribution of the automotive industry in India to the national economic development

The automotive industry is a major driver of global economic growth. It currently contributes around 6% to the world's gross domestic product (GDP). In some markets like China it's even 8%. Indeed, if the sector was a country, it would be the sixth largest economy in the world, with sales of almost USD 3.3 trillion.

The vehicle industry influences India's economy strongly

The role of the automotive industry in India is no less significant. It has seen tremendous growth over the past few years since its liberalization and plays a major part in the country's economic development. Its contribution to GDP grew from 2.8% in 1992-93 to around 7% in 2012-13, according to stats of the Department of Heavy Industries and the Society of Indian Automobile Manufacturers (SIAM).

Today, it accounts for a 22% share of the national manufacturing GDP. India's automotive industry sales in the fiscal year 2013 are estimated at USD 58 billion, plus a further USD 41 billion for the component industry. The automotive business is one of the largest job-creating industries globally, employing over 70 million people. As per SIAM, in India, 19 million people are directly or indirectly employed in the sector. This represents around 3.1% of total employment in the country and 18% of jobs in manufacturing.

According to experts, one direct job in an automotive OEM creates five indirect jobs in the "automotive ecosystem". In addition to a wide range of component suppliers and sales dealers, this ecosystem includes a number of other companies, ranging from raw material suppliers to machinery and capital good suppliers, plus services companies in areas such as logistics, transportation, automotive finance, advertising and maintenance. Moreover, the presence of automotive clusters in or near cities gives a substantial boost to companies in areas such as real estate, construction, consumer goods, food and beverages, education and so on.

The automotive industry is also responsible for a significant share of foreign direct investment (FDI) in India. According to the Department of Industrial Policy and Promotion, automotive FDI showed a compound annual growth rate (CAGR) of 18% between 2008 and 2012, accounting for 6.7% of total FDI inflow into India in the fiscal year 2013. All of the world's major OEMs and tier 1 suppliers are present in India. They have contributed significantly by setting up world-class manufacturing plants and bringing advanced automotive and components R&D and technology to India.

Indian manufacturers are entering the global market

Indian automakers such as Tata and Mahindra now own global brands. In addition, companies such as Hyundai, Maruti Suzuki, Ford, Renault Nissan, Bajaj Auto and Hero Moto Corp all are exporting from India. With a large base of very small cars ("A segment"), excellent cost competitiveness and frugal research and development, India is rapidly becoming a global hub for the development and manufacture of compact cars. The automotive industry has achieved world-class quality, as demonstrated, for example, by the Indian-made Hyundai i10 and i20, mostly exported to mature markets in Western Europe and Australia.

Domestic growth, increasing competition and the adoption of international standards have created a world-class auto component supplier industry in India. According to the Automotive Component Manufacturers Association ACMA, domestic auto component sales saw a CAGR of 12% between the fiscal years 2008 and 2013, up from USD 26.6 billion to 40.6 billion. Component exports saw a 22% CAGR from USD 3.8 billion to 9.3 billion in the same period.

Almost all large global suppliers are present in India, including Bosch, Continental, Magna, Faurecia, GKN Driveline and Tenneco. Most have set up their R&D and offshore engineering centers here. In addition, successful Indian automotive suppliers have achieved global scale through a combination of organic and inorganic growth. Players such as Bharat Forge, Motherson Sumi, Amtek and many others continue to expand their global footprint through major acquisitions outside their home country. Imports doubled from USD 6.2 billion to 13.1 billion in this timeframe.

The Indian automotive component industry currently exports over 60% of its products to developed markets. Imports, by contrast, stem mainly from Asia. The depreciation of the Indian rupee creates a significant localization opportunity for the component sector.

The vehicle industry has given identity to several areas of India

OEMs and suppliers drive excellence in manufacturing across the industry – and beyond. Their best practices in areas such as just-in-time, quality and productivity are followed by many other industries, having a positive impact on the entire country. Good management practices such as Lean, Six Sigma, TQM, TPM, JIT, First Time Right, the Failure Mode Effect Analysis (FMEA) and the Theory of Constraints (TOC) have become everyday language in large companies as well as small and medium enterprises across India. Most OEMs and large suppliers also invest in building the skills and have enhanced potential of their entire workforce. Indeed, it is widely acknowledged that automotive companies provide one of the best training grounds for employees and have produced excellent professionals and a highly trained workforce.

As elsewhere in the world, the Indian automotive industry is based around well-defined clusters, concentrated geographical regions in which interconnected companies create an ecosystem of innovation and productivity.

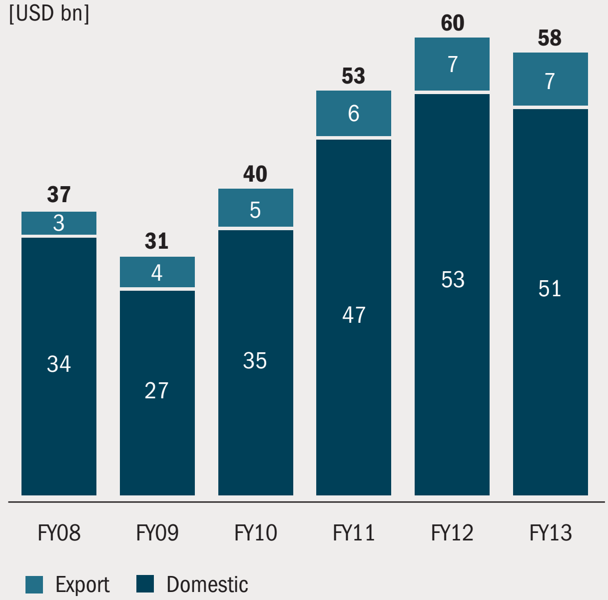
In this way, the automotive industry has given an identity to areas such as the National Capital Region (NCR), which includes Delhi and adjoining urban areas, and Uttaranchal in the north of India, Pune-Aurangabad-Nasik and Gujarat in the west, and Chennai-Bangalore-Hosur-Coimbatore in the south. Clusters increase productivity, stimulate innovation and facilitate commercialization and entrepreneurship. According to the Institute of Competitiveness, states with a portfolio of related clusters such as Maharashtra, Tamil Nadu and Delhi show higher levels of prosperity than others.

Global automotive markets – current challenges

The automotive industry is facing a number of significant challenges – both in India and beyond. It saw a dramatic

ANNUAL SALES OF INDIA'S VEHICLE INDUSTRY ARE ABOUT USD 100 BILLION – THAT'S TWICE THE AMOUNT COMPARED TO 2009

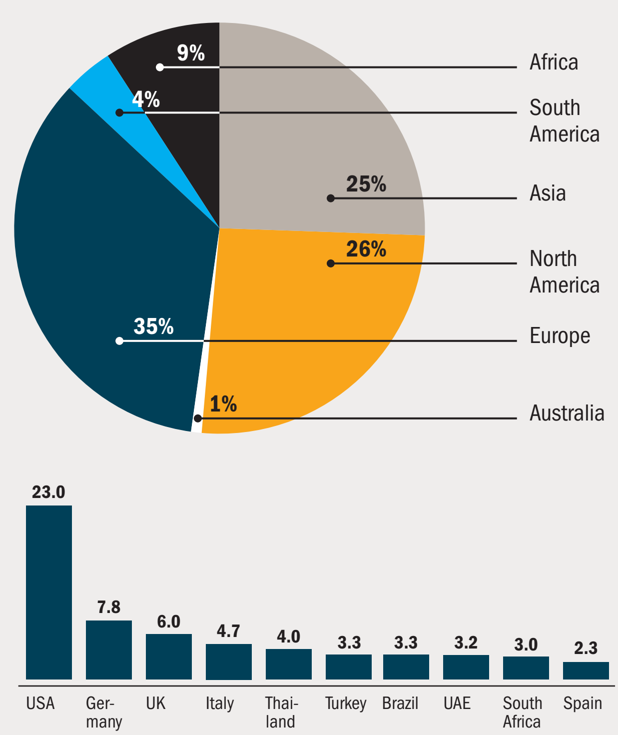
Sales of the automotive industry
[USD bn]



Source: SIAM data, Roland Berger analysis

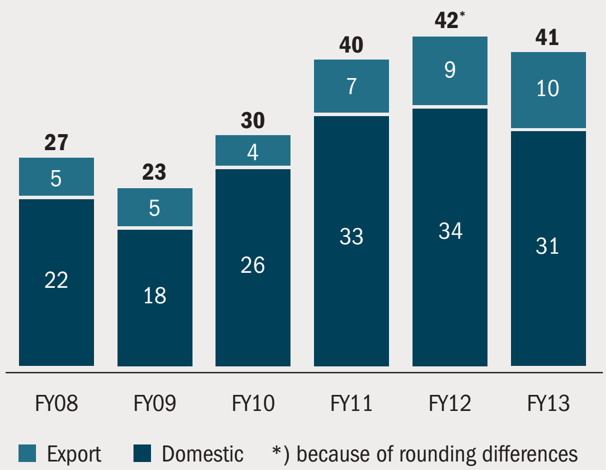
INDIA'S AUTOMOTIVE INDUSTRY IS A GLOBAL PLAYER. 60% OF ITS PRODUCTS ARE DELIVERED IN DEVELOPED MARKETS

Destination of auto component exports FY13 [%]

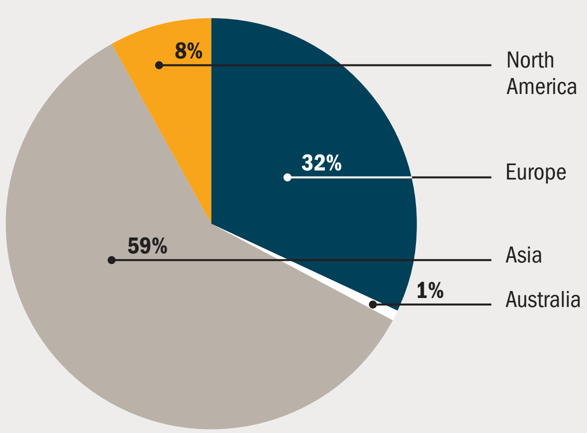


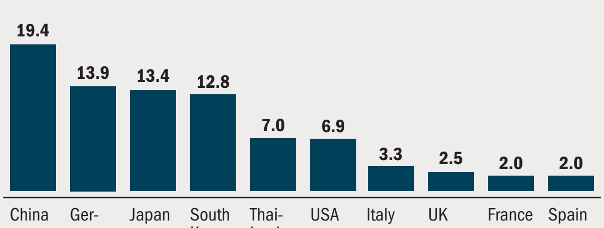
Source: ACMA

Sales of the component industry
[USD bn]



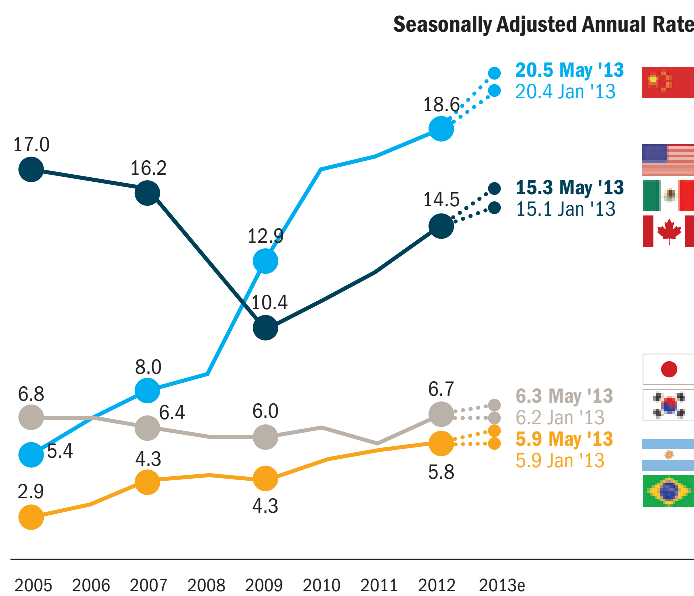
Source of auto component imports FY13 [%]





contraction in demand during the financial crisis in 2008. Sales dropped and OEM and supplier plants were shut down for extended periods of time. The collapse in sales around the globe led to various government interventions in the automotive sector, ranging from bailouts and subsidies to policy-level interventions to boost consumer sentiment and create buying momentum. From traditional economic powerhouses such as the United States, Japan and Germany to emerging growth engines such as China and Brazil,

LIGHT VEHICLE SALES BY REGION IN MILLION UNITS:
GLOBAL SALES ADDED UP TO 80 MILLION IN 2012 AND ARE EXPECTED TO GROW TO 83 MILLION BY 2013



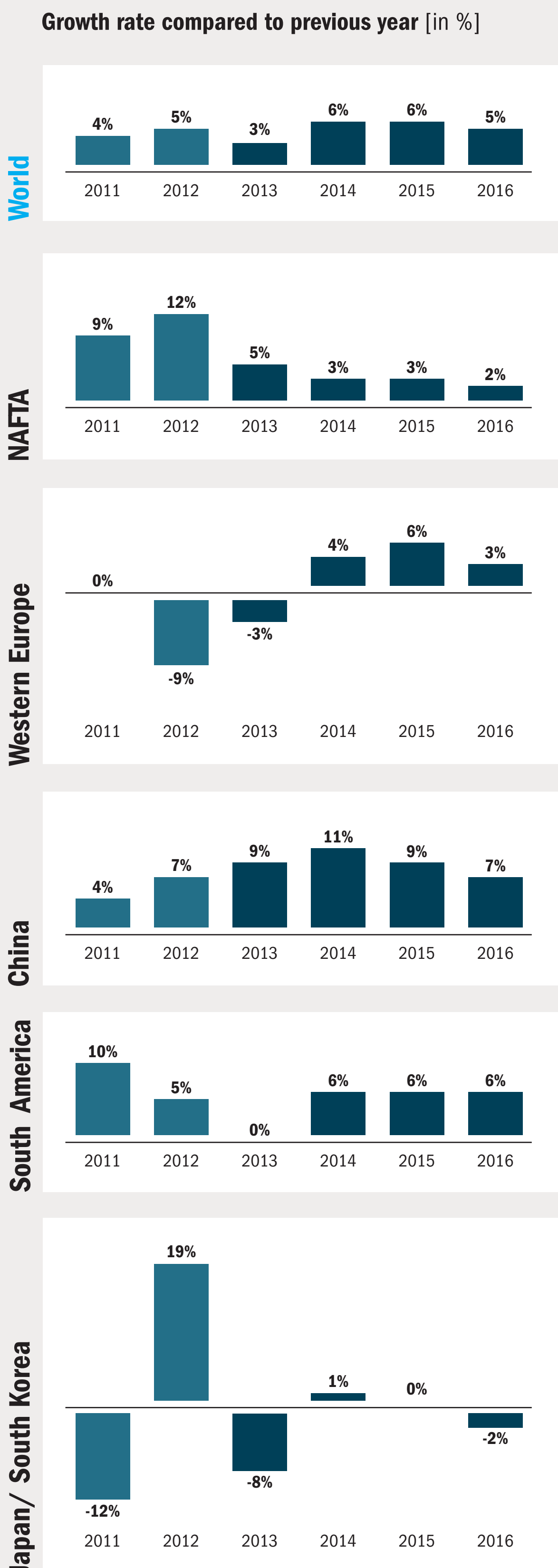
Source: IHS, Roland Berger analysis

governments and policymakers played a critical role in reviving the industry.

At a macroeconomic level, car purchase incentives cushioned the decline to some extent. As a result, global sales of light vehicles recovered after the crisis much faster than expected. This recovery was particularly strong in China, the NAFTA states, Japan, Korea, Russia and Brazil *(see infographic above)*.

The, year 2013 was difficult in terms of sales of passenger vehicles for Western Europe, Japan, Korea and India. Going forward, however, the industry is expecting to see good growth from 2014 onward.

MAP OF PASSENGER VEHICLES SALES[1]. GLOBAL SALES ARE EXPECTED TO GROW BY 3-6 PERCENT PER ANNUM BY 2016



1) Incl. light commercial vehicles

■ forecast

Source: IHS, Roland Berger analysis

India's current slowdown: Short-term crisis or long-term opportunity?

Currently, India's overall economic growth is slowing, with no immediate recovery in sight. Due to persistent inflation, rising twin deficits and a depreciating rupee, the GDP growth rate fell from 9.6% in 2010 to around 5.8% in 2013. The crisis is further heightened by supply-side constraints, lack of reforms, power and coal shortages, stopping of various mining and other industrial projects, and a significant deterioration of the country's global image due to retrospective legal amendments and various scams in the area of governance. Added to this, as per Institute of Competitiveness, India fell to 59th place (out of 144) in the 2013 global competitiveness ranking, down from 56th in 2012. India is losing its edge as a cost-competitive manufacturing destination.

The economic downturn, the general slowdown in the manufacturing sector, fuel price corrections, rising inflation and high interest rates have all had a negative effect on aspiring automotive buyers. The ratio of fuel price to per capita income is exceptionally high in India: 30 times higher than in the US, for instance, and still 3 to 10 times higher than in the other BRIC markets China, Brazil and Russia. In addition, the recent hike in diesel prices and excise duty on SUVs has negatively impacted growth. The industry sentiment in the automotive sector is currently at an all-time low, with underutilized capacity, production cuts, a slowing down of expansion plans and (more recently) layoffs.

Sales of domestic passenger vehicles (PV) were down 7.5% in the second quarter of 2013 compared to 2012. OEMs are running at low capacity utilization and have started laying off temporary workers.

Sales of medium and heavy commercial vehicles (MHCV) – a cyclical industry directly linked to the growth of the index of industrial production – have fallen almost to their 2010 levels. Domestic MHCV sales were down almost 17% in the second quarter of 2013 compared to 2012. Commercial vehicle OEMs are running at very low capacity utilization and shutting down for longer periods.

The massive slowdown that is engulfing MHCV sales has started to impact sales of light commercial vehicles (LCV) too. The domestic LCV goods segment which grew at a brisk pace since last few years, de-grew by almost 6% in the second quarter of 2013 compared to 2012, indicating that the weak macro situation has now

India is a tremendously growing nation: by 2025 its population will have surpassed the Chinese one

started to percolate to the last mile transport segment also. Growth in the high-volume two-wheeler segment has also slowed down. Overall, domestic two-wheeler sales in the second quarter of 2013 were marginally down on 2012.

As a result of the slowdown, most experts have revised their earlier forecasts for the Indian automotive industry. Sales projections for domestic PV sales in 2020 have been reduced from nine to five million – a drop of almost 45%.

Demographics – both opportunity and greatest challenge

It's not all bad news, however. As global population increases to around eight billion in 2025, India will become the country with the world's biggest population. 1.46 billion inhabitants will mean even 64 million more than China or more than 18% of the global total in 2025. India will also continue to have a highly favorable demographic pyramid compared to other countries.

India's urban population will increase by about 160 million people by 2025 – a growth of more than 40%. This share will have significant needs for mobility and transportation and thus represents a large potential automotive market. Moreover, India currently has the world's lowest car penetration and thus significant growth potential. The number of 18 motor vehicles per 1,000 people is only a fraction compared to other nations: Even emerging markets like China (85 per 1,000) or Brazil (249) have a much higher penetration – mature countries like the US (797 per 1,000) or Japan (591) anyhow.

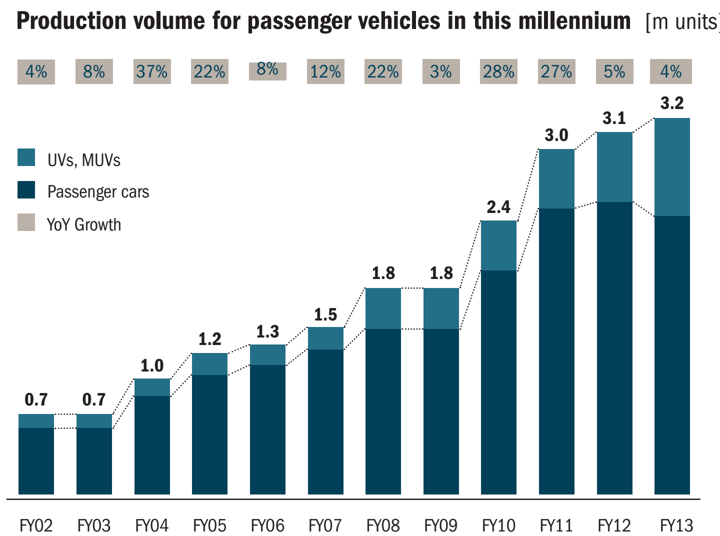
The size of India's labor force is set to increase by around one million people every month. Given the current economic outlook, a prolonged slowdown will be very detrimental to India. If the country is unable to provide employment opportunities, the demographic dividend will become a problem.

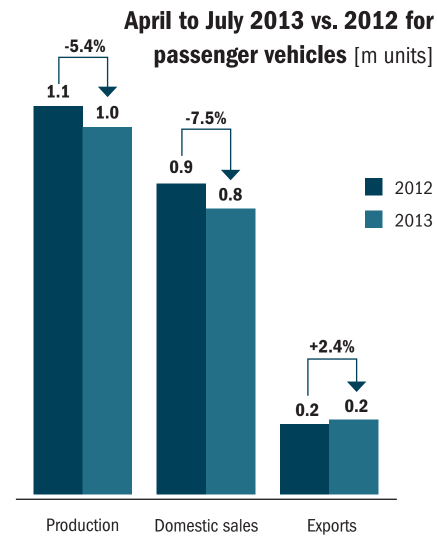
What should India do to deal with the challenges it faces and maximize its very real opportunities? How can it revive momentum in the economy in general and the automotive industry in particular? There is widespread confidence across the industry that recovery is possible – the question is: How?

Learning from Germany's transformation

From 1995 to 2005, Germany had the lowest average GDP growth rate (1.3% per annum, compared to 2.3 in the EU-15, for example) and the highest unemployment rate in the Eurozone. This significantly reduced the country's competitiveness. However, structural reforms carried out between 2000 and 2005 resulted in little short

LONG-LASTING GROWTH FOLLOWED BY A RAPID DECLINE: THE PRODUCTION VOLUME OF VEHICLES IN INDIA FLUCTUATED STRONGLY IN THE LAST YEARS





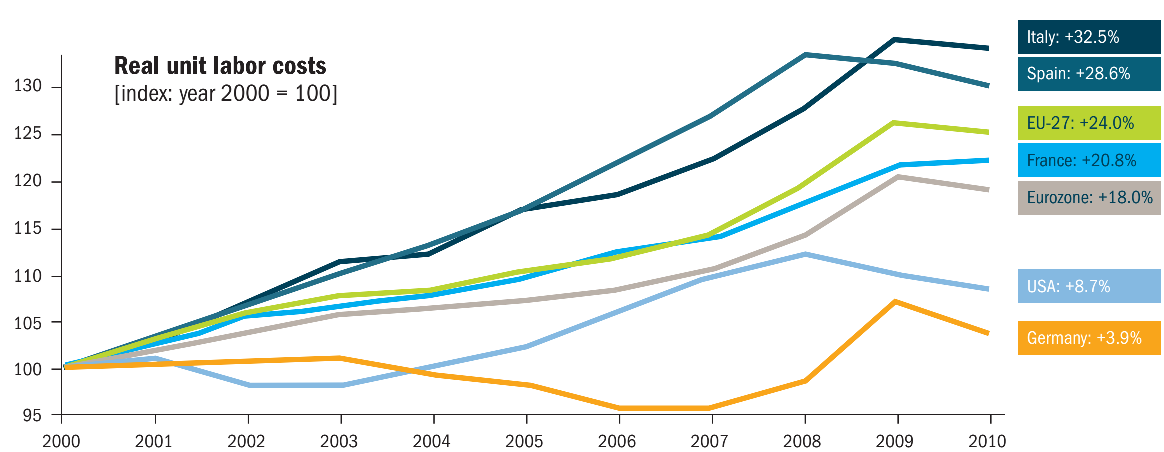
Source: SIAM data, Roland Berger analysis

of an economic miracle. Post-reform Germany became a high-growth economy, creating a political framework for the superior competitiveness of its business as well as for growth, employment and the creation and distribution of wealth. Germany's GDP growth per capita is even more impressive, as the population shrank compared to other countries with continuous population growth like the US.

In its structural reforms of 2000 to 2005, Germany worked relentlessly to reduce red tape, implement public and private financial discipline and reduce the public sector share of GDP. The country implemented productivity-oriented labor agreements, provided for dismissal protection and created flexibility in labor markets in the area of minimum wages, flexible working, pensions and welfare benefits. In addition, it encouraged significant investment in R&D and technological innovation in carefully chosen industries.

The productivity-oriented labor agreements between unions and employers increased the country's competitiveness both globally and within the EU. This also meant that the increase in real unit labor costs was only slight in Germany compared to the US as well as to France and other Eurozone countries.

GERMAN ROLE MODEL: REAL UNIT LABOR COSTS IN GERMANY GREW BY LESS THAN FOUR PERCENT IN THE FIRST DECADE OF THIS MILLENNIUM. THAT HELPED TO MAKE THE ECONOMY MORE COMPETITIVE



Source: OECD, Roland Berger analysis

Optimistic outlook: Despite the current weakness, the future of India's auto industry remains promising

Germany focused on superior innovation to meet the demands of emerging markets. This approach gave the country the largest share of research- and knowledge-intensive industries in the world by 2007 in terms of gross value added. With its R&D-oriented business culture, Germany was the only European country among the top 10 nations that exported to China.

Finally, the devaluation of the euro against the dollar and German devaluation compared to other Eurozone countries – the result of cost-containing political reforms and business transformation – led to huge trade and current account surpluses in Germany.

These processes, combined with constant efforts by the German automotive industry in the areas of productivity and R&D, enabled automakers to increase their share of the European market to 28% (up by 3%). The EBIT of German automotive groups as a percentage of revenue was much higher than their French counterparts. The attractiveness of the country for manufacturing also enhanced: 40% of global output by OEMs came from Germany in 2011 compared to 31% from France. German automotive stakeholders gained from the growing competitiveness and favorable business cycle.

Transforming "incredible India" into "credible India"

Action is needed to make India's story credible again. Faith in governance and policy must be rebuilt, India must become an easy, preferred and competitive destination for business, and investment and consumption sentiment must be boosted. Softening interest rates and a revival in consumer sentiment will help stop the current recession in the automotive industry. Political stability – hopefully possible from the second quarter of 2014 – should boost confidence across the economy. In addition continued reforms and focus on implementation is needed to achieve higher growth in the Indian economy and the automotive sector.

We believe a number of steps can be taken to put India back on a path of high growth, create jobs and revive industry in general:

- Reestablish the credibility of the India story by continuing reforms, communicating the vision, approach and action plans across sectors globally and within India, and boldly address factors that have eroded the confidence of foreign and domestic investors

- Stick to a long-term, growth-oriented, stable policy roadmap across all industries
- Restart stalled projects and carefully monitor their implementation; fast-track long-awaited reforms such as the Goods and Services Tax (GST) and the Direct Taxes Code (DTC); create a long-term roadmap for removing supply-side constraints
- Invest significantly and consistently in infrastructure development, both physical and social; boost the investment cycle by means of major public expenditure and innovative public-private partnerships
- Boost overall consumption sentiment by implementing pro-growth interest rates and tax policies; incentivize the movement of savings from gold and real estate to productive sectors of the economy
- Address the problem of the twin deficits through consistent action, fiscal discipline (potentially unpopular), bring down unproductive public expenditure and increase the productivity and accountability of public expenditure
- Implement labor-market reforms, provide support and incentives to job-creating industries and create innovative apprenticeship and skill-building programs
- Provide impetus to India's exporting sectors (given the significant depreciation of the rupee)
- Invest in institution-building where there are problems of governance, transparency, conflict or corruption
- Develop India's vision for different sectors and communicate the same in India and beyond, backed up with concrete actions; ensure effective communication to all levels of society

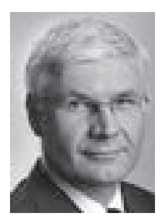
How to boost growth in India's automotive industry once again

In addition, some specific actions can bring the revival of growth in the automotive industry. We see seven needs:

- Review the excise duty structure; evaluate automotive industry demand related to reduction of taxes and duties
- Reduce interest rates on loans for vehicles or provide incentives in the form of tax rebates or registration cost rebates on the purchase of new vehicles
- Continue investment in public transport fleets
- Communicate a clear long-term roadmap for vehicle emissions, fuel efficiency and safety standards to enable investment planning by industry
- Push reforms and regulations for fleet and vehicle modernization – by scrappage incentive and end-of-life of vehicle regulations, for example
- Strengthen road safety infrastructure and enforcement with means like vehicle inspection centers and weighbridges to check overloading; discourage the overloading of trucks and overcrowding of buses
- Encourage hybrid and electric mobility, providing front-end policy support for innovative automotive technologies

With the correct actions, we believe India can use the current downturn as an opportunity to create a fast track to revival. The results will take time, but there is widespread confidence in the potential of the economy in general and the consumer and automotive industry in particular. The automotive industry plays a vital role in driving economic growth, including job creation, GDP, prosperity and competitiveness. Reviving it should be a priority for the next chapter in India's growth story.

AUTHORS



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ROLE OF MARKETING

It's a long and expensive way from the very first sketch to the finished vehicle. So the pressure to succeed is high

KNOW YOUR CUSTOMER– BUILD BETTER CARS

Why strategic marketing must take the leading role in product development and work as peers with engineers and designers

All vehicle manufacturers want their models to be successful, but launching new cars is a risky business. There is often only a fine line between success and failure, and a new vehicle introduction may determine whether a company takes the lead or falls behind in the highly competitive car market. Many examples have met customer expectations and translated into positive sales figures. Just think of the VW Golf, the BMW 3 Series or the Porsche 911.

Decisions about the product portfolio therefore need to be made very carefully and depend on several factors: different customer preferences, general demand in the market, the company's own strategy (or proposed strategy) and the preferred/available technology. Ideally, these decisions are made in established product development processes by the relevant committees and are usually well structured in terms of responsibilities and timescale. But according to our market insights and experience at Roland Berger, day-to-day business rarely lives up to this ideal. These decision-making procedures are not always handled in an ideal way and often leave out one important type of stakeholder: marketing experts, in their role as product strategists.

WE SEE THREE STRATEGIC PILLARS TO SET-UP THE RIGHT PROCESSES AND TO CHOOSE THE APPROPRIATE TOOLS

	1 MARKET ANALYSIS	2 DESIGN BRIEFING	3 COMMITTEE STRUCTURE
DESCRIPTION	Define one methodology to analyse the market and its dynamic	Translate results of market analysis into the "language" of the design and engineering departments	Strategic marketing must take the lead in product development process both content-wise and from an organizational perspective
CONTENT	Nine steps help to create a comprehensive analysis 1. Clear mission 2. Target segment 3. Target group 4. Segment attractiveness 5. Competition 6. Customer perception 7. Migration analysis 8. Determining characteristics 9. Pricing	Design briefing comprises three perspectives 1. Communicate results clearly and authoritatively to the stakeholders 2. Backup results with solid data 3. Apply specific tools for evaluation (e.g. customer clinics)	Install marketing as first among equals in cross-functional committees (including R&D, IT, Quality, etc.) Recognize possible conflicts as early as possible Come to a consensus, which finally can be presented to the executive board as long as all content related questions are answered
OUTCOME	One methodology as company wide standard Clearly defined product requirements based on extensive evidence based market research	Elaborated and comprehensive briefing to provide design and engineering stakeholder with an overview about customer needs	Install strategic marketing as "primus inter pares" Strategic marketing makes decisions and presents recommendations to the executive board

Source: Roland Berger

Will this model meet the demands of future drivers? This question has to be the leitmotif of the entire production

Customer demand has to be the first priority

This kind of collaboration is not simply an optional extra, but one of the fundamental processes in vehicle development. If customer expectations and the corresponding product requirements are not analyzed in the early phases or – even worse – analyzed but not communicated effectively to engineers and designers, model launches may well be unsuccessful, to the detriment of profit, market share and image. In addition, this may lead to resources being deployed ineffectively in the development process, with engineers working on projects that customers do not want.

To ensure successful launches, strategic marketing must lead from the very beginning, deriving and clearly defining product requirements based on extensive evidence-based market research. The results should be carefully translated into specific product requirements that are understood and fully accepted by designers and engineers. Strategic marketing should be first among equals in the process of developing new vehicles and should focus fully on the product and brand alignment.

Our article explains how to set up the right processes and choose the right tools – to ensure satisfied customers and to build better cars.

Top or flop: It's not just about the money

The cost of developing a vehicle starts at USD 1 billion. For a completely new car on a newly developed platform, the cost can be as much as USD 6 billion. That's more than the annual sales of some listed corporations. Besides the direct costs, new product launches tie up large amounts of human capital, especially precious engineering expertise, for a long period. The time needed to develop a new model ranges from 24 to 54 months – not including the preparation time before project execution (pre-PEP phase).

Car development teams often consist of a few hundred engineers split into teams working on chassis and body, suspension, drivetrain, control systems and other major subsystems. And what do all of these engineers do? They devise solutions and test them until they get it right. But are they always testing the right things? Are these tested features really appreciated by the customers?

In addition, these projects tie up engineering capacity and thus engineers cannot be deployed to develop other, possibly more profitable or sustainable projects. In an industry as competitive as the car industry, that's a huge strategic disadvantage. Besides, there's nothing more demotivating for high potentials than working for months or even years on a project that ends up being shelved. In other words, huge amounts of money, time and productive human capital are being spent on something customers do not currently value.

The Audi A2, for example, seemed to be a smart idea and won over internal and external experts, but still did not achieve the forecast sales figures. Audi wanted to offer an affordable entry point into the premium segment. From an engineering perspective, the car was ahead of its time. Unfortunately, full plant capacity was never reached and Audi stopped production in 2005. Audi needed several years to successfully reenter the compact car market with the subsequent A1. Interestingly, the A2 is now in great demand in the market for pre-owned cars, as it now meets customers' needs. This is of course no consolation for Audi.

All stakeholders in the process have to speak the same language

Failed launches are a no-go in the highly competitive automotive industry – we have already mentioned the negative impact on image, market share and sales figures. But how can marketing expertise be integrated into the product development process from the very beginning? Two aspects matter: Both are strategic aspects, one is content, the other organization. Content-wise, it is crucial to define one methodology to analyze the market and its dynamics. This methodology then ought to be used as mandatory standard in the company, across all departments. All analyses should be based on this methodology, resulting in reliable and universally accepted data.

From an organizational perspective it is important to include all stakeholders in the process, to speak the same language and to set up a committee structure with clear tasks and responsibilities, with strategic marketing leading the decision-making process.

NINE STEPS HELP TO CREATE A COMPREHENSIVE ANALYSIS FOR EVERY NEW VEHICLE

Designers and engineers can only build the right cars, if marketing supports them with the results of the customer analyses

1 | Mission

First of all, you need a clear vision for a model. To define its mission, first produce a comprehensive summary of the product, its (desired) USP, roughly outline the target segment and groups and the key characteristics. Based on these insights, define the car's strategic role. This role depends on a handful of factors: long-term objectives of the company, the positioning of this particular vehicle in relation to other models of the brand, customer needs and the competition.

2 | Target segment

Clearly define the target segment to fit the new product into the brand's portfolio. Do this for each market relevant to the brand, including design and technical aspects as well as the planned marketing strategy and pricing.

3 | Target group

Who will buy our car? That's the core question of this analysis, which focuses on the social status and the value orientation of future customers. The first aspect refers to buying power. The latter can be separated into the classic range of values from traditional to avant-garde or post-modern. The range can easily be visualized by two typical groups: On the one hand, there are blue collar workers with very traditional values who are mainly interested in lower-priced, practical cars. Daily usability of the car has first priority. On the other hand, there are postmodernists with high social status who value self-realization and who are interested in new technological concepts such as smart mobility or gadget connectivity.

4 | Segment attractiveness

Next, analyze the volume and growth of your intended segment. Annual growth ratefigures and the development of competitors' sales volumes help you assess the potential of your own car. As most new cars are designed to be rolled out internationally, perform the analysis for every target market. There are several established alternatives such as Sigma or our Roland Berger Profiler as well as internal company sources. Define a single method for all business units to ensure uniform, comparable and reliable results.

5 | Competition

Thoroughly research competitor models in the same and adjacent segments. This helps you determine the market potential for your own car. Most vehicles have four kinds of competitors:

- Models in the same category (direct competitors)
- Cars of the same type that are higher-priced but still affordable by the target groups (or at least a relevant share of them)
- Similar cars that are lower-priced and with lower specification
- A broader competitive environment with other kinds of cars that might be interesting alternatives for customers

6 | Customer perception

This step of the analysis is based on grid mapping, which helps determine target customer perception in several categories. These can be, for example, family- or budget-oriented, sporty or conservative. There is no universal list; interesting attributes have to be worked out individually. Bear in mind that these characteristics are not mutually exclusive; you can apply multiple characteristics. To analyze the data, compare the characteristics against those of existing models, successors and competitors. The approach is also helpful in mapping new concepts for new models in the pre-PEP phase.

7 | Migration analysis

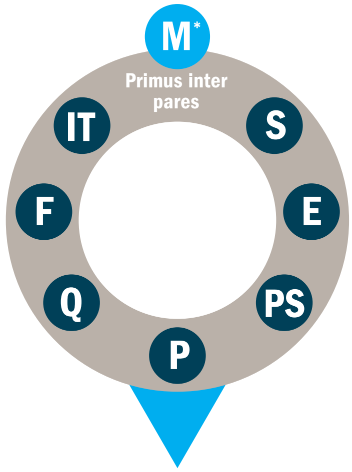
This analysis aims to identify relevant customer migration from one brand to other brands as well as from one model to other models. It is usually based on customer interviews and helps predict future gains and losses of market share. Migration analysis is thus a powerful tool for evaluating the potential of new concepts.

8 | Determining characteristics

To develop a successful vehicle, it is absolutely vital to determine its characteristics and be clear about its functional interaction. These characteristics include all future sales angles. The range of characteristics varies depending on the brand and the car, but some aspects like design, price, usability, safety, driving performance and quality are crucial in every development process.

THREE CRUCIAL STEPS IN THE PRODUCT DEVELOPMENT PROCESS: FROM AN ORGANIZATIONAL POINT OF VIEW, MARKETING HAS TO BE THE FIRST AMONG EQUALS IN WHOLE DECISION-FINDING

1. **CONSTITUTION OF A CROSS-FUNCTIONAL EXPERT COMMITTEE**



2. **PRIMUS INTER PARES IN DECISION MAKING PROCESS**

Tasks of strategic marketing:
- Recognize possible conflicts as early as possible (product perspective vs. brand perspective within the development process)
- Clarify strategic, financial or sales issues
- Come to a consensus, which finally can be presented to the board

3. **RECOMMENDATIONS TO THE EXECUTIVE BOARD**

Tasks of strategic marketing:
- Presenting recommendations to the board as soon as all content related questions are answered

*) E = Engineering, F = Finance, IT = Information technology, M = Marketing, P = Purchasing, PS = Product strategy, Q = Quality, S = Sales

Source: Roland Berger

One tried-and-tested method of illustrating these characteristics is the radar chart.

Depending on the type of vehicle, the different characteristics may have to be analyzed in more or less detail. Driving performance includes details like the engine sound, seating position, traction and many others.

To understand the car's expected strengths and weaknesses, its characteristics can be superimposed on a similar chart with attributes of comparable competitors' models. By doing so, advantages and disadvantages can be easily visualized. Thus, the radar chart (if drawn up properly) is a powerful tool and can be used to support the entire product development process. Combined with other data – on customers, for instance – it provides all stakeholders with reliable and understandable information on the actual development status of the new model.

9 | Pricing

The final step in comprehensive market research is to determine the target price. The pricing position should be analyzed in relation to the internal and external situation. The basket includes all other models of the group in sub-segments or sub-brands if applicable. The latter refers to the competitor basket.

How to translate the results into specific product requirements

These nine steps together produce a comprehensive analysis. Next, the strategic marketing department must translate the results into specific product requirements that are understood and accepted by the design and engineering departments. This is done in the form of a detailed, standardized design briefing, written in the language of the designers and engineers. Its main aim is to improve the link between marketing, product strategy and design, and thus lay the foundation for a sustainable solution. It gives all stakeholders an overview of customer needs in the pre-PEP and PEP phase.

If this goal is missed, the process comes to a standstill, as happens in many car companies. Substantial market research is done, but the results are either not forwarded to the designers and engineers or – what's almost as bad – not translated appropriately into their language.

In the briefing, all results must be communicated clearly and authoritatively so that all stakeholders understand them and take them on board. The results should be backed up with solid data and the briefing should clearly define all relevant design aspects in sufficient detail. Furthermore, criteria for evaluating and assessing design prototypes must be clear and universally accepted. For this purpose, the characteristic radar chart combined with the hierarchization of the different attributes is a very useful tool.

Finally, the design briefing must be backed up by specific tools and methods such as customer clinics, buying pattern analysis and design guidelines.

The organizational point of view

As mentioned above, strategic marketing must take the lead in product development both content-wise and from an organizational point of view. In this step, the strategic marketing department makes decisions and presents recommendations to the executive board, as long as all content-related questions are answered in depth and based on reliable, proven and accepted analyses.

Cross-functional committees usually make the key decisions about new product launches and new developments. They usually consist of experts from various business units including R&D, IT, quality management, and marketing & sales. Strategic marketing people not only work as peers with designers and engineers, they must actually assume leadership in these committees to enable valuable solutions.

Decision-making in the product development process is highly complex and we highly recommend viewing the strategic marketing department as first among equals in this process. The core task is to recognize possible conflicts as early as possible, for instance when the process seems to be driven from a product perspective instead of from a brand perspective, or to clarify strategic, financial or sales issues (Will the sales and service network be able to accompany the rollout in all relevant markets? What about the necessary marketing resources? Are repair shops equipped with the appropriate technology, etc.?) and to come to a consensus which finally can be presented to the board.

Reliable, in-depth market research from the very start of the process, as well as translating the results, will lead to the "right" car being made and will help set up the necessary organizational and procedural steps along the way.

Marketing has the power to build better cars

Changes in the automotive landscape have never been as fast as today: Product development cycles and technological progress are accelerating and customers' needs are becoming more individual and fast-changing. This leads to a higher risk of flops. And these flops are increasingly unwanted as OEMs battle for market share and margins in a competitive environment that is fiercer than ever before.

In our view, the only way to avoid flops is to give the strategic marketing department a leading role in product development. It should be considered first among equals in the relevant cross-functional committees. And it must clearly define and communicate binding product requirements based on a strict focus on customer value. To build better cars, create satisfied customers and boost margins.

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AUTOMOTIVE TRENDS

"What particularly impressed me last year was the number of new technologies launched – these were highlighted especially at the trade shows, both by OEMs and suppliers. Vehicle functions that have been discussed and researched in the automotive industry for years are now out on the streets."

Marcus Berret
Partner

"Fascination for the automobile is still alive, despite the economic crisis in the major markets and regulations on CO^2 and mobility. Design, technology and innovation – these formerly independent stimulators of the markets have merged. They are making cars safer, greener and cheaper, and turning them into high-tech luxury goods with increasingly eco-centered DNA. The automotive industry is reinventing itself once again."

Ralf Kalmbach
Partner

"Despite all the innovation in electric mobility, connectivity and technology, the product remains king. This was the message of the various trade shows, especially the IAA – which, by the way, impressively demonstrated the confidence of a strong industry in challenging times. This return to focusing on the product is coupled with a strong rebound of car design. We also saw initial signs of some brands' return to former glory last year – competition will be tougher and more interesting."

Ralf Landmann
Partner

"In 2013, a lot of vehicles with new and innovative technologies appeared on the road – from new, alternative powertrains and modern materials (e.g. composites) to new connectivity solutions. Every OEM needs to face the fact that technology is becoming increasingly complex and no one can develop everything on their own. This means partnerships and alliances will become even more important in the future."

Wolfgang Bernhart
Partner

LAST YEAR'S TRENDS AND FORECAST FOR 2014 – THAT'S WHAT OUR EXPERTS THINK

"The cars of tomorrow have taken shape last year: They will have control panels with large touch screens for media, communication and many control mechanisms – technologies we already know from smartphones."

Norbert Dressler
Partner

"The challenges for the industry are clear: It's becoming harder to stand out from the competition, customers are increasingly favoring individual solutions and it's still not certain which powertrain technology will ultimately prevail."

Marcus Hoffmann
Partner

"A key insight in 2013 was that electric mobility can also be fun for premium customers. The BMW i3 and the Tesla Model S are the best proof of this."

Philipp Grosse Kleimann
Partner

"Connected vehicles will certainly reshape the automotive landscape in the years to come – new applications, new players and new business opportunities. Autonomous driving also proves that the automotive industry has the power to turn visions into reality."

Jürgen Reers
Partner

"After years of discussion, electric mobility has finally arrived on the road – to me, this is one of the key messages for the automotive sector in 2013."

Thomas Schlick
Partner

"Connectivity, e-mobility and growth in emerging markets are still the key topics in our industry"

Marcus Berret, Partner

INSIGHTS Mr. Berret, looking back at 2013 in the automotive business, what have been the hottest topics?

MARCUS BERRET We have seen two main drivers of innovation: electric mobility and advanced driver assistance systems. Both dominated the headlines and the big trade shows, and are becoming more and more visible in the showrooms of manufacturers and suppliers, of course.

Sounds promising! But EVs still account for under 0.2% of new registrations in Germany, correct?

You are absolutely right. But the foundation has been laid. At the IAA, everybody could see that electric mobility is well on its way to becoming reality. If I compare the situation with the 2011 fair, this time the concepts and new EV models are much more realistic and in line with current market needs. By the end of 2014, German OEMs alone will have launched more than 15 electric series models in all segments, from small and compact to sports cars. Just look at BMW's new i3, for instance, which was launched in November. That's the important news: The OEMs are no longer just making announcements, they now have the actual products in their showrooms.

Many OEMs believe that the mass market implementation of e-mobility is going to be a marathon, not a sprint. Do you agree?

For sure! The volumes of battery-driven electric vehicles will remain rather low for some years to come – also because the traditional propulsion engine still has a lot of improvement potential. But as I said earlier: the fact that a broader portfolio of vehicles is now available will help a lot.

You mentioned advanced driver systems as the second hot topic of 2013 besides e-mobility. What insights can you share with us?

Well, it's pretty clear that connectivity and advanced driver assistance systems will be some of the fastest growing product segments over the next few years. Many innovations such as automated parking, semi-automated driving up to certain speeds or intelligent night vision are already on the road – and consumers like these features. They make our cars safer, more comfortable and often even more fuel-efficient. And a lot more is in the works. However, we need to be careful not to over-hype these technologies. Every couple of years, our industry exaggerates expectations on a specific topic. Ten years ago, this was the first telematics wave. Four to five years ago we had the electric drive hype. Currently everybody believes that we will all have automated driving in our cars very soon. This will not happen. In our industry, technology trends mostly take longer than expected to be actually "on the road" in large volumes.

One final question, Mr. Berret: what's your view on the development of emerging markets?
In the past few years, the most fascinating development was of course the Chinese market. In 2013 alone, Chinese consumers will have bought more than 15 million vehicles, making China the largest single market in the world. This is of course pretty obvious. However, the development of the other BRIC markets – Brazil, Russia and India – is much less clear. All three markets faced significant drops in volume in 2013 compared to 2012. Russia and India, for instance, declined by 7% in 2013. Don't get me wrong: of course I'm convinced that all these markets will be key markets for the auto industry in the future, as they are for some brands even today. But the high volatility of the markets is creating a lot of headaches for many OEMs and their suppliers. As a consequence, many of them are in restructuring mode in some of these markets. The key thing to watch for over the next couple of years is whether China remains as stable as it has been over the past few years. If yes, then our industry will continue to grow favorably.

■

Marcus Berret, Partner of Roland Berger Strategy Consultants, is in charge of the company's automotive activities in Germany. In addition, he manages the consultancy's global business with automotive suppliers. His client base includes over 100 suppliers around the world and he has worked for half of the world's 50 leading suppliers. Before joining Roland Berger, Berret studied business administration in Stuttgart and Paris. He has also worked for several large industrial corporations.

STRATEGY

FLEET MANAGEMENT

CHALLENG
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BRIC MAR


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KETS

As the European fleet business becomes increasingly demanding, OEMs are looking to emerging markets for growth opportunities. But can they achieve success in BRIC markets by applying tried-and-tested concepts?

Since Europe is still going through tough economic times and the automotive market outlook has only moderate prospects, OEMs are looking beyond the crisis-troubled continent when it comes to long-term growth opportunities. Particularly, the BRIC countries (Brazil, Russia, India, China) and other emerging markets continue to be interesting *(see figure at the right)*. Obviously, the BRIC markets are on everyone's agenda due to their enormous potential, despite a recent slowdown in economic growth.

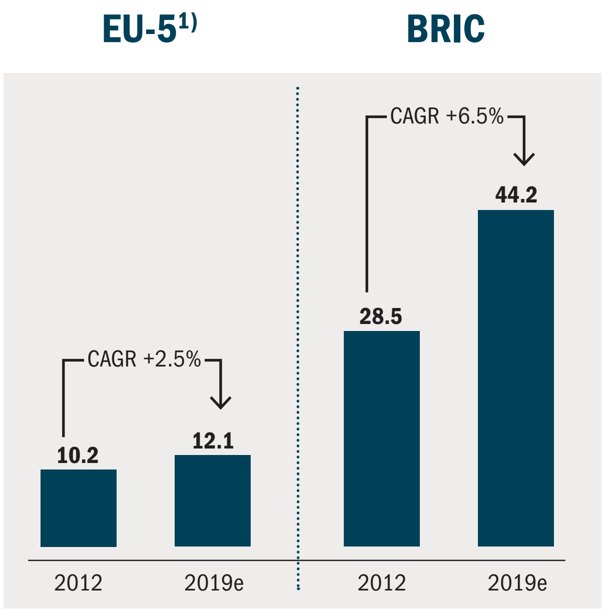
However, if OEMs wish to be successful in these markets, they have to play by local rules. This also applies to the fleet business. Below we explain the challenges OEMs may face in these countries and set out ways of overcoming them.

Undeniably, selling to corporate clients is an important sales channel for OEMs, as it provides predictable and stable revenue streams compared with private customers. In Europe, the fleet business is well established and, depending on a country's maturity, accounts for up to 60% of total sales volume. Yet, because of the high incentive levels, poor residual values and a difficult market outlook, OEMs are looking for fleet growth opportunities beyond the increasingly challenging European markets. While the share of fleet sales in BRIC countries is still lower (26% in Brazil and 9% in China, for instance), it is by no means a negligible segment *(see figure on page 35)*.

On the contrary, we believe that fleet business in the emerging markets is on the verge of becoming more developed and needs to be addressed with market-specific strategies now. But can OEMs simply transfer

HUGE GAP: EXPECTED GROWTH RATES IN THE VEHICLE SALES ARE MORE THAN TWICE AS HIGH IN THE BRIC MARKETS AS IN THE EU-5 COUNTRIES

Total light vehicles sales volume 2012-2019e
[m units]



1) The EU-5 countries are France, Germany, Italy, Spain und UK

Source: IHS, Roland Berger

tried-and-tested concepts from Europe and automatically be successful in the BRICs? Or do they need to adapt their expertise from a successful domestic business model to account for local differences?

Based on our project experience in established and emerging markets, we have found key factors that drive successful OEMs' fleet business and analyzed to what extent they are applicable in the BRIC markets.

A professional fleet business always depends on a successful balance between three stakeholders: fleet customers, dealers and OEMs. Fleet customers are a diverse group: large corporate clients, small enterprises, public institutions, rental, leasing and taxi companies, and even associations. This results in a complex customer landscape.

The dealer network sells and services vehicles for this multi-faceted group, meeting each customer's specific requirements. The OEM's wholesale organization steers and supports the dealer network in its efforts to acquire fleet customers; at the same time it can sell directly to certain important customer groups.

Key practices for success

Within this nexus of customers, dealers and the wholesale organization, we observe that market-leading OEMs in mature markets adhere to nine key practices to achieve success:

1 Execute a clear segmentation strategy

OEMs define strategic goals, set policies and assign areas of responsibility to dealers and their central key account teams. In addition, they define distinct guidelines for each target customer group, plus national and international customer-specific bonus agreements to ensure a well-functioning business setup. By defining key business processes, they avoid uncoordinated customer acquisition.

2 Maintain an extensive network of fleet-oriented dealers

Only a few large customers purchase directly from OEMs, and most small to medium-sized companies acquire vehicles from dealerships. Thus fleet-trained sales staff is needed in the showrooms. In the purest form, it means having a dedicated retail format with internal standards in place, such as fleet business centers.

3 Support and motivate the dealers

Field consultants support and motivate dealers by identifying regional sales potential for lead generation. Ideally, their resources are fully dedicated to fleet.

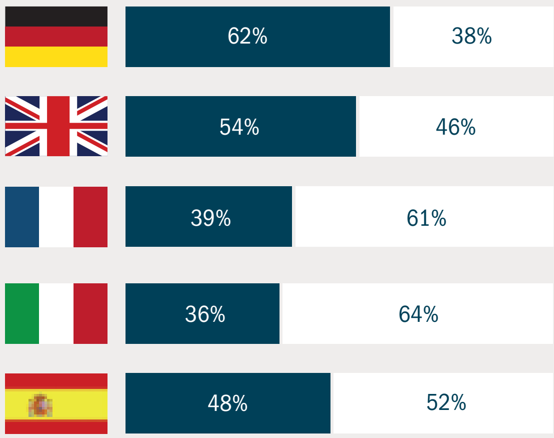
4 Measure dealers according to agreed targets

Dealers are measured by agreed targets and held accountable for their sales performance through

ENORMOUS GROWTH POTENTIAL IN BRIC:
THE SHARE OF FLEET SALES STILL LAGS BEHIND THE FIGURES IN MATURE EUROPEAN MARKETS

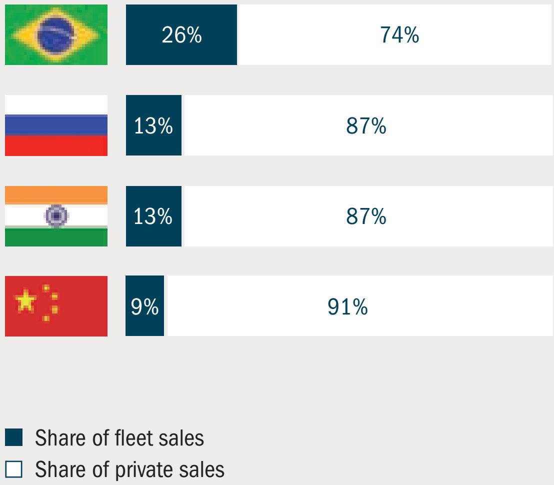
ESTIMATED SHARE OF FLEET SALES IN 2012

EU-5[1)]



1) Including rentals, dealers and OEM registrations

BRIC



Source: Dataforce, National Information Center, Roland Berger consistent performance management. Correspondingly, the budget spending of national sales companies (NSCs) has to be measured as well.

5 Create and communicate intelligent pricing policies

Intelligent pricing policies determine the profitability of the fleet business and the fast provision of quotations. Highly successful OEMs are aware of the potential behind orders from corporate clients, treating discounts to new customers for smaller orders as investments in future sales.

6 Establish fleet sales as a distinct function

Establishing fleet as a distinct function in the wholesale organization is the most fundamental step to ensure fulfillment of fleet's cross-departmental tasks. It has to ensure that all fleet-specific activities are either conducted internally or coordinated through an interface with a relevant department.

7 Conduct fleet-specific marketing activities

A fleet department should ideally be in charge of dedicated fleet marketing to increase corporate sales leads. It develops a fleet brand and campaigns while supporting the corresponding dealers in reaching regional fleet customers.

8 Develop aftersales and services

Developing aftersales as well as financial services and benefits can increase client loyalty and the number of throughputs.

9 Manage key accounts professionally

Key accounts are managed through professional customer relationship management and the right focus is set when targeting new prospects.

BRIC: Less developed structures mean room for development

Successful OEMs enforce these key practices in most European countries, while others still have room to improve their processes and make their fleet operations work here. This also holds true for leading players when we look at their current status in the BRIC markets. Some may have laid the foundations for these key practices in emerging markets, but lack strategic planning, professional management or the resources to consistently market their fleet business. Besides, business-relevant used-car markets and car-financing institutions are considerably less developed.

To put it simply, the sophistication levels of the EU-5 (France, Germany, Italy, Spain, United Kingdom) and BRIC differ. By and large, fleet operations in the EU-5 have progressed so far that they can operate successfully in saturated markets. In the BRICs, by contrast, many of the aforementioned practices are much less developed, but the markets offer opportunities and room for development.

Which car for which user? OEMs need well-trained dealers at the point of sale

Key questions that OEMs need to answer

In pushing the fleet business and tapping the potential of BRIC markets, managers face specific challenges and must answer a set of key questions:

WHO ARE THE FLEET CUSTOMERS IN THE BRICS AND HOW SHOULD WE APPROACH THEM?

As with any business, the basis for excellent customer segmentation in fleet is a data-driven analysis of segments and purchasing behaviors to understand a market's demand dynamics. What in theory sounds straightforward and comprehensible is in practice a true challenge for managers in emerging countries, due to the poor quality and limited availability of reliable sales data. Or even worse, there may be disagreement on the definition of what comprises the fleet business and what does not.

→ The way to gain fundamental market know-how is often to conduct one's own primary research, promote data sharing among competitors and other stakeholders or to develop a model synthetically, reproducing the local market. Only with a sound understanding of a market's company demographics and segment sizes can OEMs reasonably define policies and market strategies. Small fleets and commercial vehicles also need to be considered.

HOW DO WE MAKE SURE THAT THE DEALERS EXECUTE OUR STRATEGY?

Within this process of policy definition, it is worth thinking about the configuration of fleet-specific retail formats (if deemed necessary) in BRIC markets. While selling through dedicated dealers specialized

FROM SEGMENTATION TO ACCOUNT MANAGEMENT: THE NINE ACTION FIELDS, OEMs HAVE TO COVER IN THE BRIC COUNTRIES

	What is the problem?	What do I need?
Segmentation and guidelines	Lack of customer insights due to poor data transparency	Conduct primary research Commit to data exchanges
Fleet-specialized dealers	Blind implementation of retail concepts of mature markets	Adapt retail concepts Develop alternative concepts
Field consultants	Low awareness and expertise for fleet business of field force	Train and incentivize field consultants Provide them with necessary tools
Performance management	Challenge to capture sales performance on dealer level	Establish reliable performance measurement system
Pricing policies	Simplistic incentive schemes leading to unexploited customer relations	Adapt advanced concepts and develop intelligent incentive schemes
Fleet organization	Lack of strategy and internal alignment Scarcity of fleet resources	Establish wholesale structures with dedicated resources and processes
Fleet marketing	Structured marketing approach for fleet missing	Derive fleet marketing plan according to local market requirements
Aftersales and financial services	Different customer requirements in aftersales and financial services	Only offer and develop services suited to local market standards
Key account management	Difficult identification of buying centers and relationship-building	Train key account managers to local market practices and implement CRM

Source: Roland Berger

in the fleet segment is common practice in Europe, it has been unusual in emerging markets up to now, with few exceptions. Are BRIC fleet customers perhaps not looking for the same customer experience as Europeans?

→ The answer to this question depends greatly on the local market requirements and circumstances. Renault in Brazil, for example, addresses the needs of business customers through its specialized Renault Pro+ network with a focus on light commercial vehicles. The introduction of such retail concepts will be a case-by-case decision depending on financial viability. Hence, OEMs have to accept market differences and apply measures that ensure a positive business case for dealers, for example by reducing the level of necessary standards and required capital. Whatever the specific retail format, training sales personnel is indispensable for increasing a network's level of expertise and professionalism.

HOW CAN WE ENSURE OUR FIELD CONSULTANTS SUPPORT DEALERS EFFECTIVELY?

Since sales to BRIC private customers have risen steadily for the past few years, field consultants have been busy supporting dealers in the core sales processes. While this has led to greater sales efficiency in the B2C segment in most cases, it has resulted in a shortage of resources and expertise for B2B sales.

→ Therefore, OEMs must bring field consultants up to speed with market-specific training in order to help dealers reach fleet sales targets. It is the task of knowledgeable field consultants to help assess the regional fleet sales potential of individual dealers in their areas. To do so, they require market intelligence tools that enable them to identify local business opportunities with corporate clients. Sophisticated tools from mature European markets will not be suitable, so innovative solutions need to be developed by OEMs and given to field consultants. Ultimately, field consultants should be responsible for managing dealers, yet in turn their commitment and motivation has to be evaluated by the respective NSC.

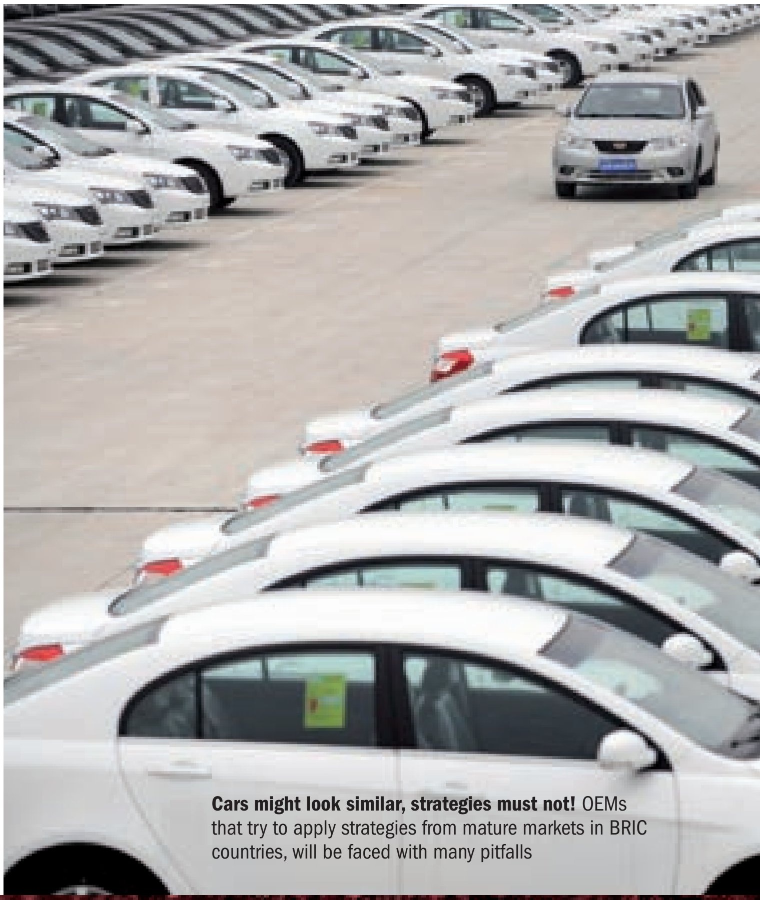
HOW DO WE MANAGE AND PROMOTE FLEET SALES PERFORMANCE?

Capturing sales performance in the market entry and development phases is crucial, not only to measure whether the strategy is being properly executed, but also to sustainably manage and incentivize sales performance. Very often, sales figures for fleet in BRICs are unavailable because they are not collected on a registration basis, and also because dealers do not separately report them to their NSC. As a consequence, performance by volume, market share or target achievement is rarely rewarded.

→ To ensure the right motivation for the fleet business, OEMs have to establish a reliable performance measurement system and incorporate KPIs such as sales volume, market share and profitability into dealer incentive systems and also into their own fleet departments. In particular, differentiation by size of fleet is important.

HOW DO WE DEFINE INCENTIVE LEVELS AND RULES?

The lower maturity of fleet in BRIC also becomes evident in the way incentive schemes of OEMs are designed: namely too simplistically. Incentive levels are solely defined by the number of vehicles purchased – the bigger the volume of a deal, the bigger the discount.



Cars might look similar, strategies must not! OEMs that try to apply strategies from mature markets in BRIC countries, will be faced with many pitfalls

However, such a scheme is unfair and obstructive, as it never truly captures a client's business potential. A client with a large fleet who buys a few vehicles of a new brand will not be rewarded for upselling potential. Experienced BRIC fleet dealers may then turn to their NSC and engage in special negotiations, which lead to extra work in the quotation department. This can be avoided in the first place through intelligent incentive schemes.

→ Here, BRICs can definitely learn from more sophisticated concepts used in Europe. In addition to volumes, they derive incentives from other factors such as fleet size, historical purchases in the last period, potential purchases in the next period, estimated brand share of the target client's fleet or even service up-selling potential. Which factors should be considered, and to what extent, must be analyzed and tested in each country. Incentives should also be defined for key accounts that have international framework agreements. Once such an incentive scheme and process has been set up, it can be highly effective and save resources. Ultimately, proper incentive management ensures a profitable and sustainable fleet business.

WHAT FUNCTIONS AND INTERNAL RESOURCES ARE NECESSARY?

Due to the interdisciplinary nature of its business, a fleet organization has to perform a broad range of tasks, while maintaining interfaces with all relevant functional departments. This requires a structured organization and distribution of responsibilities. In many NSCs in the BRICs, resources dedicated to fleet activities are scattered throughout the organization and not bundled within one department. Interfaces with other departments are not yet established, resulting in inefficient business processes.

→ OEMs would be well-advised to establish a wholesale structure with dedicated resources, a clear mission and specific responsibility for the fleet business. The detailed structure, sizing and responsibilities depend on the fleet volume, client segmentation, overall fleet strategy and each country's specific geography.

WHAT IS THE IDEAL MARKETING APPROACH FOR REACHING BRIC FLEET CUSTOMERS?

Due to unclear responsibilities or insufficient resources, there is often no structured marketing approach for the fleet segment. The featureless fleet websites of the major OEMs show just how poor the current fleet marketing efforts in BRIC markets are. In Europe, corporate customers can easily browse special offers or get quotes for their specific segment from a manufacturer's website, whereas in the BRICs, sometimes not even the contacts of the relevant fleet managers are available.

→ OEMs must either assign fleet marketing to the marketing department or build up the necessary resources to generate leads nationally. In Europe, fleet manager magazines are an appropriate channel, but in the BRIC countries they may not exist. OEMs have to look for innovative ways suited to local conditions and make sure to follow up on the leads generated. They need to set up a fleet-oriented marketing plan and support dealers in local fleet marketing.

WHAT TYPE OF AFTERSALES AND FINANCIAL SERVICES DO WE OFFER OUR FLEET CUSTOMERS?

Naturally, BRIC fleet customers, just like European ones, want to enjoy the benefits of being a corporate customer and obtain extra services. But should OEMs offer the same aftersales service packages, financial services or mobility services as in Europe, or do BRIC corporate customers value different benefits?

→ Some services in BRIC countries are mandatory as in Europe, such as preferred service hours or overnight service, while others can be optional but increase loyalty. There might be a need for new service offerings that adhere to local market standards. While in Germany, for example, over 70% of fleet contracts are leasing-based, this concept is not yet widespread in the BRICs. Hence, OEMs should be careful when offering services and first analyze BRIC fleet customer requirements with regard to aftersales and financial services. Yet, in downstream business, OEMs can really set themselves apart from the competition.

HOW CAN WE BEST SERVE BRIC KEY ACCOUNTS AND TARGET POTENTIAL CANDIDATES?

Besides professionalizing the retail network regarding fleet, OEMs must leverage their potential with large fleets of corporate clients in the BRICs. This means going beyond the strong segments of, for example, rental cars in Brazil or government vehicles in China. Cars sold to key accounts can contribute significantly to volume targets due to their large deal size. Many OEMs also underestimate the potential they have in emerging markets with domestic champions plus existing corporate clients from their home markets. The task of targeting is more difficult than in Europe because the responsible fleet managers are not as easily identifiable. They do not organize themselves into networks and often work only as third-party service providers when required.

→ In order to close deals with key accounts, OEMs first need to scale up key account resources and then train them in local market practices. Larger local corporate fleets harbor potential that needs to be investigated. OEMs should define responsibilities and prioritized processes to target new potential key accounts while providing CRM tools for customer care and service to existing clients.

Individually tailored strategies

All in all, finding the right concepts and implementing them in the BRIC markets is challenging. A one-size-fits-all approach to developing the fleet business in emerging countries will not work. Many pitfalls await OEMs that try to apply winning strategies from mature markets in countries that differ fundamentally from Europe. Yet the BRIC fleet markets offer exciting opportunities and OEMs must now decide on their fleet strategy. The key to success is understanding local requirements and industry forces. Accept the market differences and be willing to tailor your strategies accordingly.

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Books & studies

Customizing aftersales
[October 2013]

The battle in the aftermarket is heating up. While earnings from new vehicle sales are steadily declining, the aftersales business now accounts for 75-80% of the profits at many OEMs and retailers. Our study helps you find the right sales and marketing strategies for the various customer segments.

rolandberger.com/customizing_aftersales_2013

Global Automotive Supplier Study 2013
[September 2013]

Our annual supplier study has become a tradition here at Roland Berger. The latest issue provides an indication that the industry's prospects remain reasonably positive: The average profitability of suppliers is stable at an astonishingly high 6.5% EBIT margin. The study analyzes the most profitable sectors as well as business complexities and existing risks.

rolandberger.com/global_automotive_supplier_2013

E-mobility index for Q3 2013
[September 2013]

The current edition of our semiannual index rightly raises the hopes of the e-mobility industry: OEMs have been successful in developing EV technology worldwide, with vehicles now ready for series production. EV prices are thus falling sharply. In addition, the index gives an overview of the situation in the top seven countries for e-mobility.

rolandberger.com/emobility_index_q3_2013

If you are interested in older publications or future updates, please visit our AUTOMOTIVE Insights page at:
rolandberger.com/automotive_insights

Automotive Insights 02/2013
[July 2013]

How can companies succeed on the automotive aftermarket? That's the key question from the cover story of the last Automotive Insights. Our experts know the answer: It's all about tailoring offerings to the various customer groups. An in-depth analysis of the German market illustrates this approach. We also cover topics and trends from all over the automotive world: from the Chinese tire business to challenges in the US and promising opportunities in the Brazilian market.

rolandberger.com/automotive_insights_02_2013

"Rightsizing Europe"
[March 2013]

Poor prospects: 10% of jobs could be lost at automotive suppliers in Western Europe as a result of the crisis in the car industry, our study found. So suppliers' top priority is to "rightsize" their European structures. Our paper analyzes the key levers for boosting margins and sustainably improving profitability.

rolandberger.com/rightsizing_europe

Automotive Insights 01/2013
[March 2013]

The future of the supplier industry is the focal point of our March issue of Automotive Insights. Suppliers faced tougher times in 2012 after two years of outstanding growth. We discuss the current opportunities and challenges. We also look at the future of "smart mobility" and provide some food for thought on advanced driver assistance systems and discuss new relationships between OEMs and suppliers.

rolandberger.com/automotive_insights_01_2013

FAMOUS CARS

OPEL KAPITÄN

Maybe the "best Opel ever": The "Kapitän" (here the first model from 1938) was Opel's flagship model for 30 years.

Happy birthday, Captain!

What an apt name for this car: "Kapitän" is the German word for "captain". And Opel's Kapitän was the manufacturer's first mass-market model after World War II that helped navigate the company to success. The German carmaker produced the Kapitän for several decades, with the first ones rolling off the assembly lines in Rüsselsheim some 75 years ago. Happy birthday!

Developed in 1938, the Kapitän was officially launched in the spring of 1939 at the Geneva Motor Show. The pre-WWII model was famous for its unitary body, which was unique at the time. It came with a 2.5 liter engine and had a top speed of 118 kph (73 mph).

A new version of the Kapitän was launched in 1948. Initial sales were sluggish during the economic crisis of the late 40s, but that made its successes in the 50s even more pronounced. The '51 Kapitän was upgraded with a more modern body, a one-piece rear window, much more chrome and a stronger engine (58 hp). It was also a symbol of the times to come, namely the German economic miracle. It was extremely popular and became synonymous with the prosperity of 1950s. Thus, the "best Opel ever" (according to many car enthusiasts) was a must-have for the high society at the time: Owners included actors such as Heinz Rühmann and Hildegard Knef, as well as boxing champion Max Schmeling. For a while, the Kapitän was even the best-selling car in Germany (surpassed only by the VW Beetle and the Opel Olympia Rekord).

The various models were upgraded to keep pace with the times: In 1953, the updated model received a typical American-style "ponton" body and the distinctive "shark's mouth" grille. By contrast, the 60s design of the Kapitän represented the new spirit of this decade. The last model was the "Kapitän B", which was manufactured until the summer of 1970.

After production of the Kapitän had ceased, the captain's spirit lived on in the assembly lines at Rüsselsheim: Its successors, the Admiral and the Diplomat, were developed using its platform and were manufactured for seven years, until Opel released the Senator as its new flagship model in 1978.

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