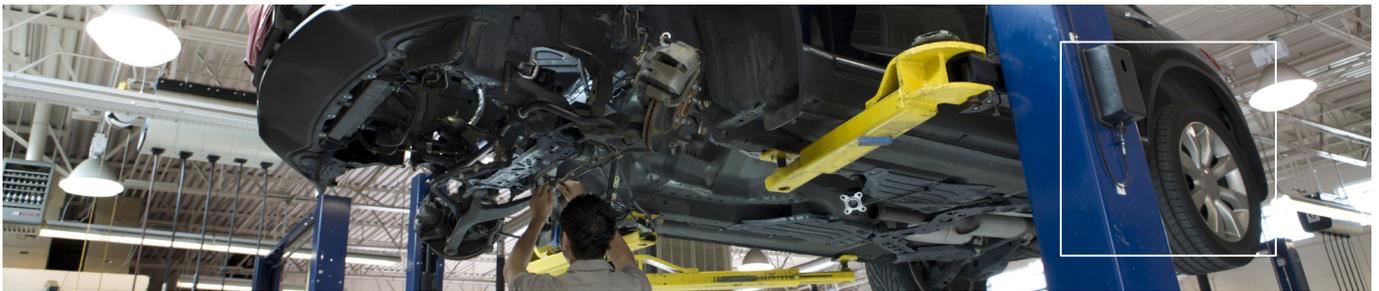


OEM After Sales Strategy

The case for innovation



With sales of new cars slowing and profit margins decreasing, after sales is becoming an increasingly important source of revenue for many OEMs. But they face stiff competition in this arena from new players intent on seizing a share of the after sales market – as already discussed in Arthur D. Little’s recent after sales INSIGHT. In order to protect and develop their after sales business, OEMs need to stop merely reacting to competitive threats and become proactive business innovators, taking advantage of disruptive new business models to regain the initiative in the after sales market. OEMs can also respond to the challenge from competitors by unlocking value in their value chain, simultaneously maximizing efficiency, supporting their brand and enhancing the customer experience.

OEMs’ after sales business is coming under increasing pressure due to growing competition, legislative changes, a shift in focus towards emerging markets and the growing differentiation in customer requirements. All these represent a major risk for OE parts & services – one of the most profitable sources of today’s automotive business. As shown in our recent study “Automotive After Sales 2015 – are you ready for the battle?“, up to 14% of global OEM after sales market share are at risk.

However, OEMs can transform this risk into an opportunity for growth by developing a robust after sales strategy. Arthur D. Little recommends OEMs begin this process by examining the disruptive after sales business models now evident in the market, and which have the capacity to change the landscape of automotive after sales in the years ahead. These new business models may become a threat to the traditional after sales strategies, but can also be a valuable growth generator for those OEMs who are able to make them part of their active strategies. Here, in order to foster really “disruptive” and creative business models, we recommend OEMs to look at those business models even before thinking about their own competences, organization and processes.

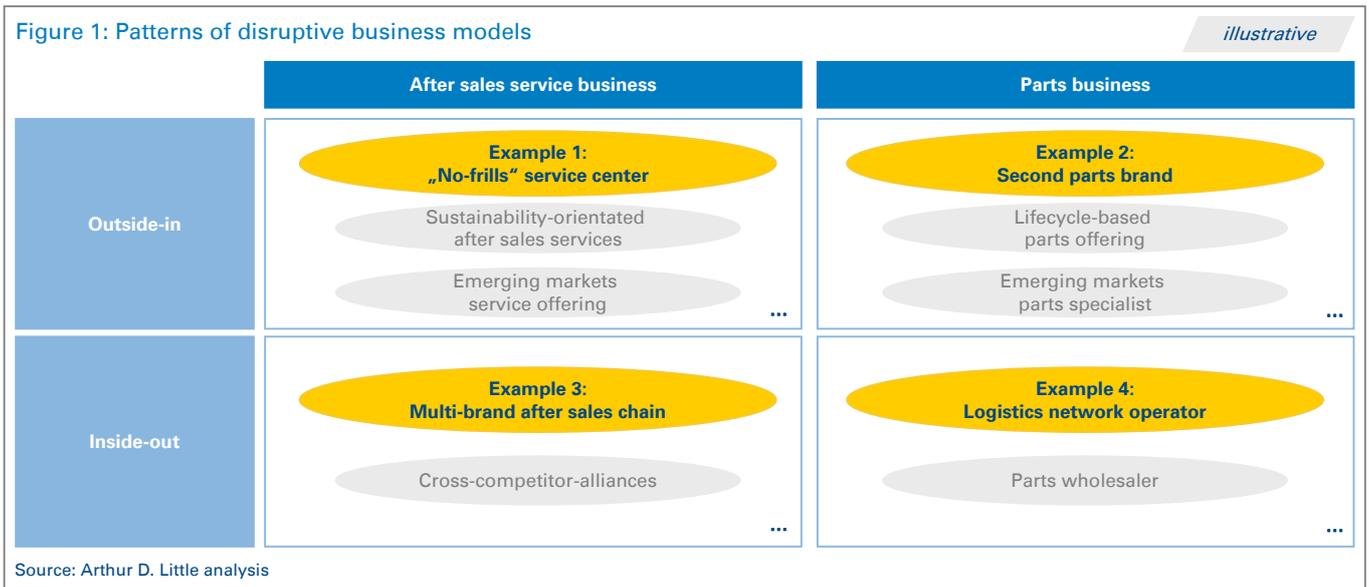
When their strategic agenda has been set for growth, OEMs also will have to enhance their competitiveness in traditional after sales operations and protect their more “traditional” after sales business. In the second half of this INSIGHT, we will hence discuss options for a new active value creation strategy,

examining opportunities across the whole after sales value chain of the OEM. Based on analysis of competitive advantage and growth potential in each step of the value chain, OEMs may unlock value in order to (re-) grow their after sales business in a very aggressive and result-orientated way.

Disruptive after sales business models – threat or opportunity?

The emergence of disruptive after sales business models has accelerated in recent years, as new service players, low-cost spare-parts providers and new alliances have entered the market. The response of OEMs has been varied, and is evident e.g. in fierce price competition and increased M&A activity. However, one aspect of the OEMs’ response has been constant: other players have acted and OEMs have re-acted. The reactionary nature of the OEMs’ response represents a major threat to their business: OEMs are adapting their strategies only once they have lost market share, by which point this element of their business may already have been lost forever.

In order to retain their role as being the driver of the after sales market, OEMs have to (re-) take the active role, developing disruptive business models all by themselves, and be the ones to surprise competitors, customers and financial markets. In this context, “disruptive” means to have a look at the global after sales markets even *before* thinking about the own positioning and competences.



In an overview of disruptive business models, Arthur D. Little provides a framework not only to analyze business models observed in the after sales market, but also to focus OEMs' own search for new ideas.

Disruptive business models can be defined from two perspectives: outside in and inside out (Figure 1). The outside-in perspective focuses on emerging or latent customer need and puts these at the center of any new strategy, regardless of the OEM's current positioning. The inside-out perspective focuses on opportunities for exploiting fully the existing after sales competencies, assets and organization of the OEM.

Analysis of the opportunities also differentiates between parts-orientated business options, such as spare parts sales, vehicle equipments, etc., and service-orientated business options, such as workshop operations and vehicle tuning.

Outside-in-perspective: What do customers need?

A wide range of disruptive business models is already shaping the after sales market. Just two of those built around customers' needs – the "No-frills" service center and a second brand for parts – are outlined below.

■ Example 1: „No-frills“ service center

Currently, most OEMs offer just one level of service, one that fits their brand promise and their price positioning for new vehicles. However, the example provided by low-cost airlines shows that there might be another option: offering a "No-frills" approach to those customers who want to spend the bare minimum to keep their vehicle going. This "bare minimum" approach should be reflected not only in the pricing, but also in the location of service centers and the level of service

provided. For example, customers would only be able to book a fixed time slot and, if they did not bring in the vehicle on time, the slot would be closed, just like a low-cost flight, with no reimbursement for the customer (Figure 2).

The branding of this service level would need to be significantly different to the branding for the full-service option. The alternative for many OEMs could be to lose their "No-frills" customers to fast-fit chains, whose growth rates show that there is a strong market demand for standardized service offerings.

■ Example 2: Second parts brand

Entering the market with a second parts brand allows OEMs to target those customers that do not use the OEMs' own after sales channels. These customers represent a growing potential market, as demonstrated by the increasing number already using low-cost, fast-fit chains for their service requirements.

Key to the success of this business model is the clear differentiation of the second parts brand and the main parts brand. Not all categories of parts would be appropriate for the second parts brand; for airbag connectors and other safety-related parts, for example, there is no scope for differentiating on quality. But for wear-and-tear parts, the option to differentiate on quality does exist. For example, a second-brand vehicle battery would be cheaper but would have a shorter life time than a main-brand battery.

OEMs will have to think about the market potential and opportunities for entering this segment, while retaining at least a part of their margin. Motorcraft (Ford), Motrio (Renault) and Eurepar (PSA) are recent examples of OEMs who have adopted the second parts brand strategy.

Figure 2: No-frills service center

Description	
 <p>Target segment: Price-conscious customers</p>	<p>Offering of products and services:</p> <ul style="list-style-type: none"> ■ Limited offering of services and parts; focus on maintenance: 3-4 standard packages (in analogy to cleaning programs in car-wash plants) ■ Customers may select original or re-conditioned parts ■ High degree of process standardization ■ Business hours 24/24, 7/7 ■ Fixed time slots, customers wait for their car <p>Price:</p> <ul style="list-style-type: none"> ■ Simple fixed prices per package ■ Cheap pricing for low season ■ Early booking rebate <p>Location:</p> <ul style="list-style-type: none"> ■ Suburbs/periphery, near highway ■ Near shopping malls, etc. ■ In combination with used-car sales operations
	<p>Sales/ Marketing:</p> <ul style="list-style-type: none"> ■ Fixed booking via Internet (or Call Center) ■ Upfront payment (cash) ■ In case of no-show, no refund ■ Branding: Second brand (“powered by...”) <p>Cooperations:</p> <ul style="list-style-type: none"> ■ Shopping mall ■ Convenience Food <p>Integration of OEM retailers:</p> <ul style="list-style-type: none"> ■ Integration in CRM ■ Interest share ■ “Transfer” and Information to relevant OEM retailer in case of “non-standard” repair needs

Source: Arthur D. Little

Inside-out-perspective: What do we do best?

The inside-out perspective on disruptive after sales business models focuses on two key questions: “What are we best at?” and “What can we do with it?”. With OEMs having established different types of after sales know-how and competency over the years, the answer will be individual to each OEM.

Two of the many examples of innovative business models founded on an inside-out perspective – the multi-brand after sales chain and the logistics network operator – are outlined below.

■ Example 3: Multi-brand after sales chain

OEM service networks have vast experience in delivering the specific after sales experience their customers want. This experience might also be used to deliver the same service experience to drivers of competitor vehicles. Stop&Go (Volkswagen) and Renault Minute are prominent examples of OEMs that have adopted this strategy. Moreover, as OEMs are very knowledgeable about the needs of customers in particular segments, they might be able to target the customers of direct competitors with a very specific service offering. For example, a Mercedes-Benz outlet could offer a premium service (e.g. a full-scope mobility package including replacement vehicle, technical service, bring-in service, etc.) also to drivers of competitor vehicles - e.g. a BMW driver. There might even be an opportunity to convince customers to change brand next time they buy a vehicle.

Multi-brand after sales chains are already forming to deliver segment-specific service offerings. The newly formed German Top Autoservice chain will target the drivers of German BMW, Mercedes-Benz and Audi vehicles more than three years old, with a very specific premium look and feel. It is clear that there will be customer-focused and segment-specific competition for any OEM adopting this strategy, either from other OEMs or new after sales players.

■ Example 4: Logistics network operator

Building and maintaining a worldwide logistics network for spare parts is a very cost-intensive operation for any OEM. Moreover, when it comes to parts, emerging markets represent a major logistics challenge. Strong growth in demand for parts, poor infrastructure, long distances and the need to cope with complex tariffs add up to create high barriers to entry for new players.

In this context, offering their logistics services to other companies might be a good way for OEMs to generate additional revenues and profit. The most prominent example of this is Caterpillar, which has used its substantial worldwide logistics experience (including the promise to deliver any required spare parts within 48 hours worldwide) to build up a very profitable logistics operation, including service contracts with direct competitors.

This business model might also be implemented in the form of a joint venture, such as Coreteam, the Chinese logistics joint venture formed in 2004 by BMW, Volkswagen and Daimler. Currently, Coreteam serves the needs of its associated OEM partners only, but could potentially become a very powerful player in the Chinese parts logistics market.

Finding the business model that fits best

The four disruptive business models shown are just starting points for OEMs aiming to develop an after sales growth strategy. Each OEM will need to think about its customers’ needs, assets and capabilities as well as market trends in order to generate a “best fit” business model. Only once a clear and market-driven after sales strategy has been defined, it is time to look at unlocking value from existing after sales processes and organization.

Unlocking value for OEMs

The general value-creation strategy adopted by OEMs – especially in Europe – is clear: only do things in-house if there is a clear and direct link to brand positioning, competitive advantage and/or core competence. In this context, the value created in-house by OEMs has declined over the years, as the example of German OEMs shows.

The picture in OEM after sales operations, however, is much less clear. Value creation strategies are often a mix of historic arrangements with key suppliers, the dominance of certain technologies and a complex network of dependency among the involved parties (e.g. retailers, OEM departments, technology specialists, service providers, etc.).

In order to establish a clearer understanding of their current value chain, OEMs need to analyze the after sales process portfolio across their whole after sales operations. The focus should be on customer perception, in order to differentiate the OEMs' after sales business from competitors, and on cost position, which is one of the major sources of competitive advantage in the global after sales markets.

Customer perception analysis can be focused on distinct customer "touch points" along the after sales value chain. These are the important moments of interaction between the OEM after sales organization and the customer. At these touch points, the OEMs' after sales organization should be prepared with best-in-class processes and brand-specific differentiators, in order to strengthen brand image and increase customer loyalty.

OEMs should ask two questions for each process: "What is the current in-house/outsourcing ratio, expressed in capacity and cost?" and "What should it be?" OEMs will find that in many

cases their value chain strategy is not aligned with customer perception or operational excellence.

Figure 3 illustrates the example of a hypothetical OEM where some differentiating processes are outsourced and other, more standard activities are covered in-house, although probably not with the best cost-efficiency. The OEM in the example undertakes the full range of diagnosis and technical information processes in-house, but lets suppliers do most of the after sales intelligence work. However, the latter is work of strategic importance in saturated markets where customer loyalty is key to sales stability and high margins.

Arthur D. Little proposes a clear, two-step methodology for analyzing each process, in order to shape a robust after sales value creation strategy.

The first step involves assigning each process to a process category, based on customer perception. So "threshold" processes, for example, are processes where there is no direct interaction with the customer, e.g. parts logistics. "Brand building" processes have a key role to play in securing competitive advantage by fulfilling the OEM's brand promise, e.g. customer reception processes at the retailer (Figure 3).

The second step involves rating the relative competitive positioning of each process, again, based on customer perception. The rating ranges from "weak" (the OEM is rated as performing less well than its direct competitors) to "strong" (the process delivers a key competitive advantage in the OEM's after sales positioning). (Figure 4).

The final step of analysis involves identifying those areas where process category and competitive position are misaligned. These are the areas where there may be new opportunities

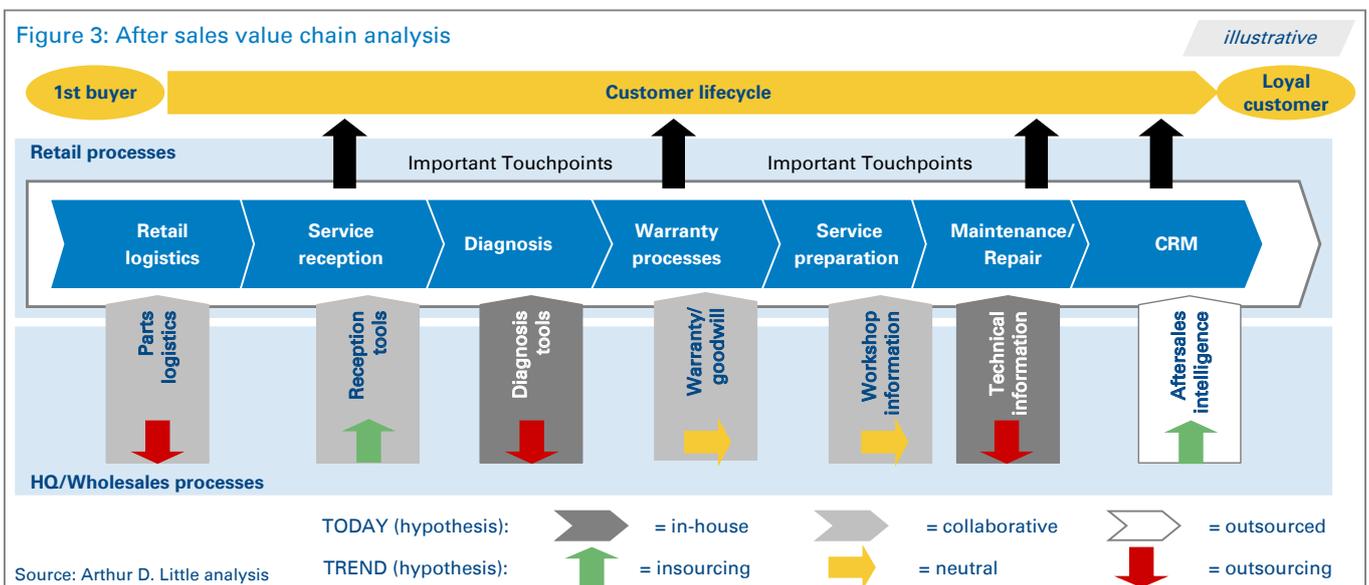
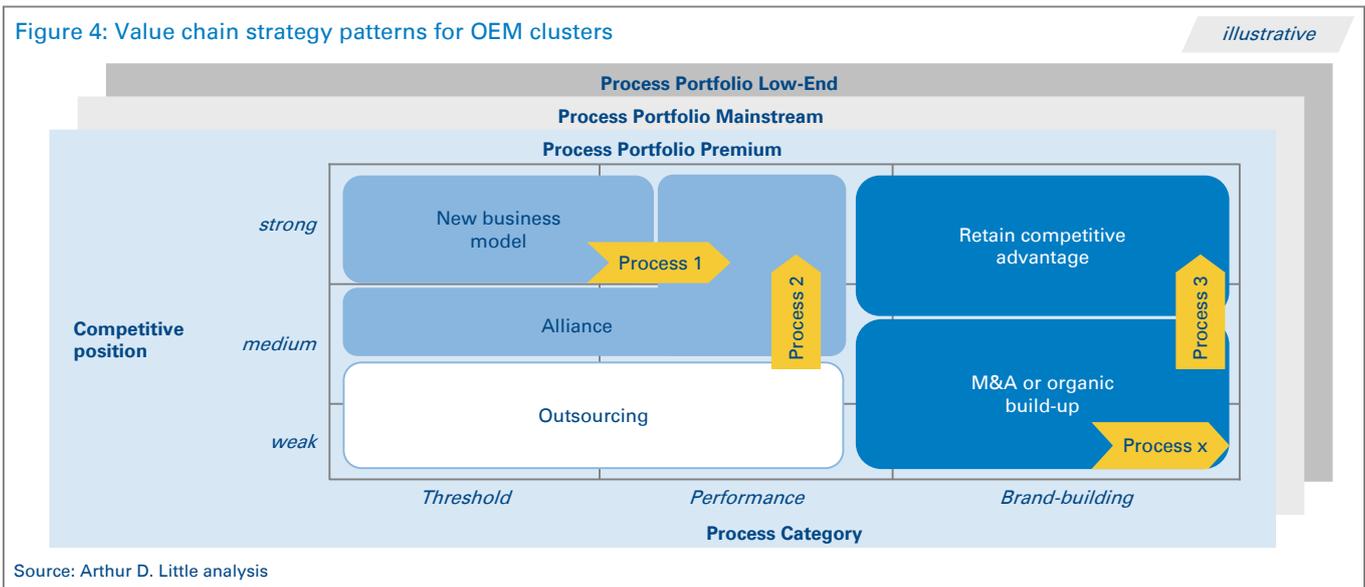


Figure 4: Value chain strategy patterns for OEM clusters

illustrative



Source: Arthur D. Little analysis

for the OEM to extract value. For example, if a process is key to brand-building in the eyes of the customer, but the OEM's competitive position is rather weak, the value delivered by this process should be increased, perhaps through M&A activity or by an organic build-up of resources and know-how. By contrast, if an OEM is strong (in terms of competitive positioning) but the process has little impact on the customer's perception of the brand, this indicates an opportunity to begin actively marketing specific competences and assets in the form of a new inside-out business model.

There is no single correct answer to the challenge of value creation for all OEMs. A premium OEM will come up with completely different answers compared to a mainstream or even a low-end OEM.

When the overall value creation strategy has been set, the next challenge will be the improvement of the competitive position in each process – meaning operational excellence in after sales. We will come back to this topic in our next after sales INSIGHT.

Conclusion

The strategic toolset developed by Arthur D. Little can help OEMs re-claim the initiative in today's dynamic after sales markets worldwide.

Business innovation, as expressed through disruptive business models, can help OEMs to grow their after sales operations and offers an alternative to the strategy of trying to protect traditional market with traditional tools. The ADL toolset helps OEMs to assess the potential of different new business models, taking as a starting point either the customer's needs or the OEM's own competencies and assets.

Establishing an active value-chain strategy can help OEMs to unlock hidden value. This strategy involves re-focusing operations on customer "touch points," in order to sharpen brand differentiation and enhance customer satisfaction while lowering cost for the OEM at the same time. The ADL toolset incorporates a framework for analyzing the process portfolio according to customer perception, competitive positioning and process categorization.

The starting point for each OEM seeking to develop an effective after sales growth strategy is different, but the challenges are common: growing competition, legislative changes, evolving customer demands and shifting geographic markets. OEMs need to begin an active discussion of where their after sales future lies and that discussion should start today. There is no time to waste.

If you would like more information or to arrange an information discussion on the issues raised here and how they affect your business, please contact:

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Arthur D. Little

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