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## Pole positioning

By Richard Spitzer

The high performers in this industry are exceptionally lean and customer-centric enterprises. But can they retain their lead as competition from emerging-market carmakers mounts?

It boasts some of the great global brands, and the influence of its innovations is felt worldwide. Lean manufacturing, for example, which is now the process and supply chain mantra for a host of industries, originated in Japanese car plants. Yet the automotive industry was struggling to turn a profit even before the sharp economic downturn in the fourth quarter of 2008 and US automakers went hat in hand to Washington.

Shorter product lifecycles, wider product ranges and soaring raw material costs—by far the biggest component of total automotive costs—are just part of the problem. Carmakers from Japan, the United States and Western Europe, known collectively as the Triad markets and long the heavyweights of the industry, are also grappling with the beginnings of a seismic shift in the sources of competitive advantage.

Americans still buy more cars than anyone else, and the Japanese remain the world's leading producers. But demand in the Triad markets was faltering even before the economic crisis—sales in those markets fell an estimated 11 percent in 2008—just as it was starting to surge in China, India and Russia, the heavyweights of the emerging economies. To be sure, the fourth quarter saw slower growth in the emerging economies than would have been expected, but demand there is still on the rise.

In many respects, of course, burgeoning demand in these important new markets is a welcome development, and a number of Triad-based carmakers are well positioned to take advantage of it. But so are growing numbers of emerging-market players.

It will be some time before these carmakers achieve the safety and emission standards that

would make Indian, Chinese and Russian vehicles a serious threat to Triad producers in their own markets. However, emerging producers are buying brands, design savvy and technology know-how from their developed-market counterparts. They also are investing heavily in R&D, and are getting better and better at innovation.

Some Triad carmakers are managing to hold the line. For example, to offset the high costs of developing the environmentally friendly vehicles consumers are demanding, some are forging alliances with traditional rivals: BMW and Daimler, for instance, are in talks that may lead to an agreement for joint purchasing as well as joint development of more efficient and less polluting power-train systems. But because no one really knows which technologies—biofuel, electric or hybrid—will turn out to be the right one for the future, these are risky investments. And it's a similar story with the Triad carmakers' efforts to turn the arrival of emerging-market players to their advantage.

Some, to be sure, have struck successful deals. The French carmaker Renault, for example, which in 1998 bought Dacia, the formerly state-owned Romanian producer, is successfully selling the popular Dacia Logan in Eastern Europe—and seems to be steadily increasing sales in Western Europe as well, where demand for smaller, more affordable vehicles is growing.

But some emerging producers have been equally successful interlopers. Consider, for example, the Indian company Tata Motors' recent purchase of the iconic Jaguar and Land Rover brands—an acquisition designed to leverage distribution networks in the Triad markets as well as to meet rapidly growing Indian demand for premium vehicles. Or consider that Chinese vehicle manufacturers may soon be supplying small cars to Triad players.

### **Extraordinary dynamics**

Only the half dozen high-performance businesses identified by Accenture research have been able to create value in such extraordinarily dynamic conditions (see “About the research,” page 3). The overall performance gap between these automotive companies and the rest of the peer group is significant. All, for example, have outstripped their peers in terms of both revenue growth and profitability.

When it comes to the first building block of high performance—market focus and position—the performance gap between these leading companies and the rest is clearer still. All the high performers have been far better than their peers at positioning the right product at the right time in the right market—particularly in emerging markets, where capturing the growth opportunity has been key to high performance.

As in other industries Accenture has studied, success in market focus and position depends much more on the quality of strategic decision making than it does on the actual size and scope of the company. Toyota, for example, dwarfs every other carmaker in terms of revenues and plainly derives considerable economies of scale from its huge size. But even more important to the Japanese company's success is its strategy of offering a wide range of vehicles, each one designed to meet specific customer needs.

Each automotive high performer has chosen to approach the markets best suited to its specific market presence, product lineup and brand positioning in a slightly different way—a choice dependent, to some extent, on its business model.

The successful mass-market players, like South Korea's Hyundai-Kia Automotive Group, have established a presence in most major markets, but

they focus primarily on selling small passenger cars in large emerging markets, where the demand for compact, affordable vehicles is especially strong (see sidebar, page 4). Some premium manufacturers, like Germany's Porsche, have successfully boosted sales not only in the world's biggest premium market, the United States, but also in emerging markets, where the appetite for luxury vehicles is particularly strong—notably, China and Russia.

### **Superior cost structure**

Distinctive capabilities, another building block of high performance, are also evident among these industry leaders. Our research found that a superior cost structure is the most distinguishing feature of the automotive high performers. This comes as no great surprise, perhaps, considering that the industry pioneered lean manufacturing. Nevertheless, the cost-effectiveness of the automotive high performers is striking indeed, and clearly the source of their ability

to create value much more successfully than their peers. As a group, they have generated consistently higher total returns to shareholders over the past seven years.

We call this distinctive capability “lean enterprise”—a combination of low material costs, flexible and demand-driven manufacturing, and back-office efficiency that together result in the exceptionally high product quality that sets the top performers apart.

All the high performers are masters of material cost management, the route to superior margins for a business that spends 60 percent of total costs on materials. Most, moreover, display outstanding process efficiency: Witness Honda Motor Co.'s reputation for engineering excellence, platform flexibility and effective vertical integration (the company even makes its own robots), or Nissan Motor Co.'s scrupulous pursuit of cost-saving opportunities.

## **About the research**

We began with a universe of 82 original equipment manufacturers and eliminated those companies that are not publicly traded, as well as those that did not provide a comparable financial data history for the last seven to 10 years. We also eliminated carmakers that produce fewer than 100,000 units annually, pure truck manufacturers and entirely local players from the set. But we included the carmakers' financial services divisions, because they are directly linked to the core automotive business and thus contribute to financial performance. (The financial services divisions' impact on revenue was 8 percent on average, and the average share of EBIT was 29 percent. However, the impact on the overall high-performance business rating is marginal.) This gave us a robust and comparable peer set of 16 companies, representing 80 percent to 90 percent of the total global vehicle market.

Accenture uses five business dimensions to measure high performance—longevity, profitability, growth, consistency and future value (which is a measure of investors' expectations about the value of a company's future cash flow). There is a negative correlation between profitability and future value for carmakers, as there is for other mature, asset-intensive, cyclical industries. So we concentrated instead on the remaining four dimensions, measuring the relative gap between outcomes to identify the high performers.

## Hyundai: Birth of a global brand

South Korea's biggest carmaker might still sell more vehicles on its home turf than anywhere else. But the Hyundai-Kia Automotive Group is already strikingly global and becoming more so. Hyundai, indeed, is the fifth largest carmaker in the world in terms of both sales and production. And remarkably, the company has managed to establish a presence in all major markets, without being overly dependent on any one of them. It is, however, Hyundai's especially robust positioning in the leading emerging markets that explains the magnitude of its success.

The Hyundai group is the third biggest player in the 3 million-car Russian market, for example, where it holds a 9 percent share. And since the company opened its first manufacturing plant in China in 2000, its presence there has grown dramatically. A joint venture with Guangzhou Motor Group in 2005 was followed, a year later, by a \$1 billion agreement with Beijing Automotive Holdings to open a second manufacturing plant in the Chinese capital. Hyundai now turns out 400,000 vehicles annually in China, nearly four times as many as in 2003. It also plans to make India a globally important manufacturing hub. Forty-five percent of the company's Indian car production is already earmarked for export to Europe, the Middle East, Latin America and Asia, and that is set to increase.

Hyundai, moreover, is keenly aware of the growth opportunities presented by particular markets and product segments, and not just in the developing world. It launched the Genesis sedan, its first premium vehicle, in the United States in 2008, for example. And the company has responded vigorously to the mounting worldwide demand for hybrid vehicles by significantly boosting its investments in technologies to reduce emissions and improve fuel efficiency.

To be sure, meeting tightening emission standards, especially in Europe, will be expensive. And rising raw material costs pose as much of a threat to Hyundai as they do to other carmakers. But Hyundai has recognized the value of lean enterprise (see story). By working directly with its supplier base to optimize material costs, Hyundai already has realized significant savings, and it expects to maintain similar savings levels through 2010. Meanwhile, strong revenues across all its geographic divisions continue to fuel the company's growth.

Lean enterprise alone, however, does not guarantee high performance. In such an intensely competitive environment, carmakers also need to capture and keep customer loyalty. And Accenture research reveals that customer-centricity, the second distinctive capability of high performers in this industry, sustains the reputation for swift and superior service as well as an engaging, multi-channel retail experience that is also a hallmark of the leading carmakers. Customer-centricity hinges, moreover, on being able to deliver leading-edge options such as Bluetooth connectivity, sophisticated in-car entertainment systems like flat-screen displays in headrests that keep kids occupied on long journeys, voice-activated controls and other technologies that customers value.

### Balancing act

Being customer-centric and lean at the same time is challenging for all carmakers, including the high

performers. Achieving that balance may be easier for a relatively small, premium carmaker like Porsche, which has a knack for aligning rapid, customer-driven product and service development with an optimal retail and service experience (see sidebar, page 5). But some of the mass-market players have also been astonishingly good at developing products aligned with market trends and specific customer segments.

Toyota, for example, pioneered the first mass-produced hybrid car in response to growing demand for fuel-efficient and environmentally friendly vehicles. And Honda's CR-V or Nissan's Qashqai are innovative and attractive answers to specific customer demand for so-called crossovers—the smaller, more fuel-efficient versions of once-popular sport utility vehicles, which borrow features like four-wheel drive but are built on car rather than truck frames.

## Porsche: Maintaining the cachet

There are many reasons for Porsche's success in creating one of the most prestigious automotive brands in the world. Among the most important, however, must surely be the exceptionally solicitous way the company treats its customers.

All new Porsche owners are offered a free "track day" before they receive their vehicle, for example. There, instructed by professional drivers, they get to drive a variety of Porsche cars on a racetrack that replicates Formula One driving conditions. Porsche also spends more time and effort than other manufacturers explaining the particulars of each new vehicle for its owner—an investment that not only maintains the cachet for which its vehicles are so famous but also builds tremendous customer loyalty.

These practices, indeed, personalize and deepen the customer experience—an essential aspect of the customer-centricity that Accenture research has identified as one of two distinctive capabilities among high performers in the automotive industry (see story). But Porsche is equally good at the other distinctive capability: lean enterprise. In fact, constant optimization of

commercial processes, coupled with consistently high levels of customer service, ensure that the German company is in a position to exploit all market opportunities.

Porsche can dispense with the need for vehicle discounts precisely because it's so good at constantly analyzing individual market developments, shifting production quotas and adjusting manufacturing to prevent inventory from reaching critical levels. These measures, moreover, add still more to product value: Even pre-owned Porsches maintain their value.

As far as Wendelin Wiedeking, the company's charismatic and hands-on CEO, is concerned, Porsche's prosperity vindicates his conviction that the customer is king. "When the customer is happy then the worker is happy, too, and so are the suppliers," he once told an interviewer. Shareholders take something of a backseat in Wiedeking's view, as they do for many employers in a country where industrial cooperation and consensus are considered the foundations of sound business practice. But for Porsche's shareholders, at any rate, that poses no problem.

All the high performers execute better than their competitors, a function of their strong, centralized leaderships and exceptional talent management. These qualities are both attributes of performance anatomy, the third building block of high performance, although each high performer projects quite a different version of such a winning mindset.

### Superior execution

Suzuki Motor Corporation, which retains strong links with its founding family, has a rather conservative image; Honda prides itself on being flexible and innovative. Porsche, meanwhile, cultivates a bold and independent image. Moreover, Porsche is consistently ranked among Germany's top three employers, thanks to the exceptionally generous bonus programs and benefits packages it provides for all employees, which not only lure top talent but also retain it by encouraging and rewarding contin-

uous improvement. Toyota, too, is known to develop and retain the best talent—and not only in Japan. Witness the recent opening of the Toyota Technical Training Institute in Bangalore, India.

Today's high performers will require these skills in abundance in the future, when all players will be challenged to sustain a globally balanced market presence in a multipolar world. Profitable growth will continue to be driven by selling the right products in the right market at the right time, of course. And being present in key emerging markets like China, India and Russia will be essential. But not all vehicle segments in each of these markets will continue to offer attractive growth opportunities. Small and compact cars remain the strongest growing segments globally, for example, but in the Indian market, demand for micro vehicles is expected to predominate.

Moreover, today's leading carmakers will have to recognize that the seizure of market share in emerging markets, however successful it was in the past, is largely a one-off exercise, especially as homegrown competitors gather momentum. High-performance businesses will have to evaluate the specific country and segment combi-

nations that best suit their individual product and sales profile even more carefully in the future, and align their portfolios accordingly. Those decisions will vary from business model to business model. But new sources of competition from rapidly emerging carmakers seem certain to complicate the choice.

## About the author

Richard Spitzer is the global managing director for Accenture Automotive and Industrial Equipment. In this capacity, Mr. Spitzer, along with his global leadership team, sets the company's strategy for serving the global automotive and industrial equipment industries, helping clients become high-performance businesses. Mr. Spitzer is based in Houston.

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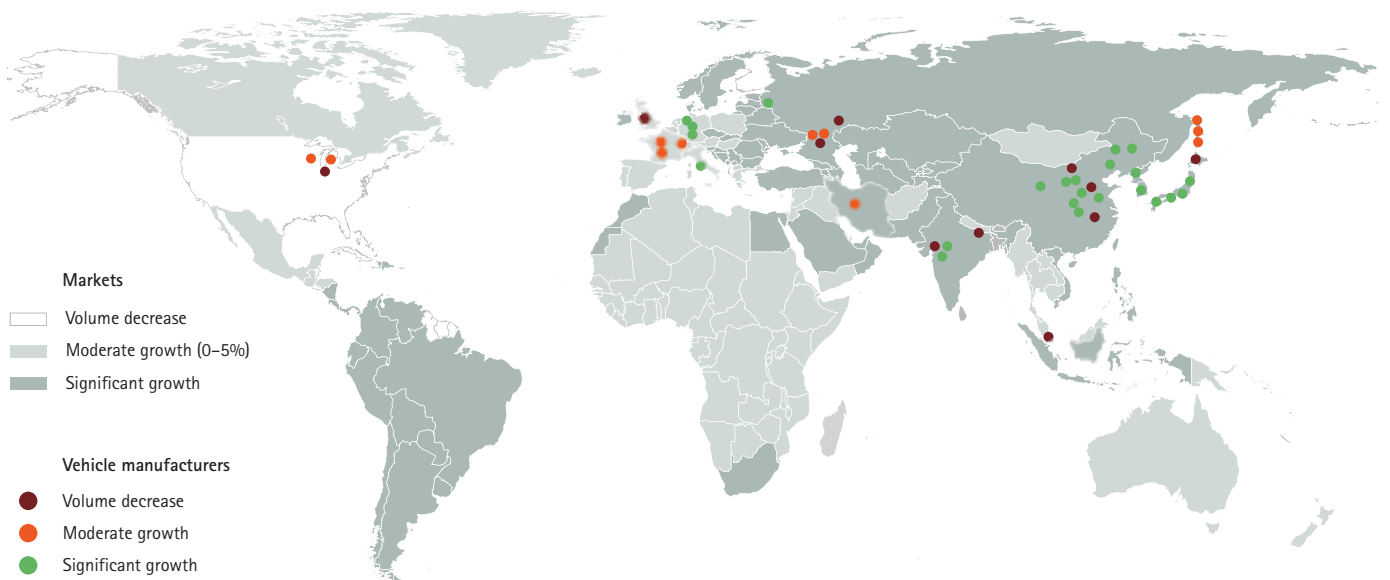
## By the numbers

# Bumpy road

Although the auto industry is currently being pummeled, looking at what was occurring in the industry through 2007 can provide indications of the direction the industry can be expected to take once the current crisis subsides.

The automotive landscape was changing up through 2007: Sales in the traditional Triad markets (the United States, Western Europe and Japan)\* were stagnant, compared with robust sales in emerging markets.

Markets and players, 2003–2007

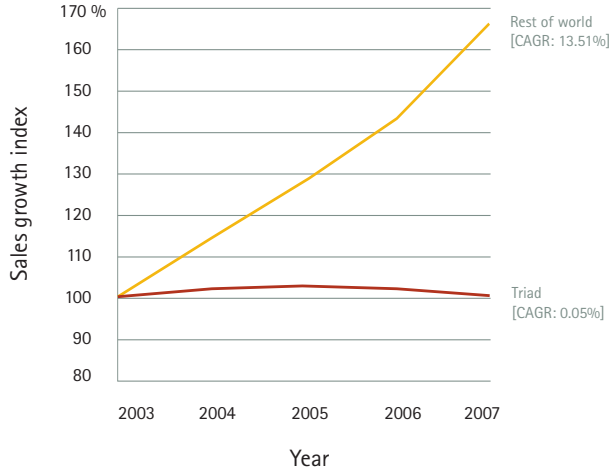


\* Excludes heavy commercial vehicles and OEMs with fewer than 5,000 units in 2003.  
Source: Global Insight, September 2008; Accenture analysis

In fact, from 2003 to 2007, sales\* grew at a compound annual growth rate of 13.51 percent in the non-Triad countries.

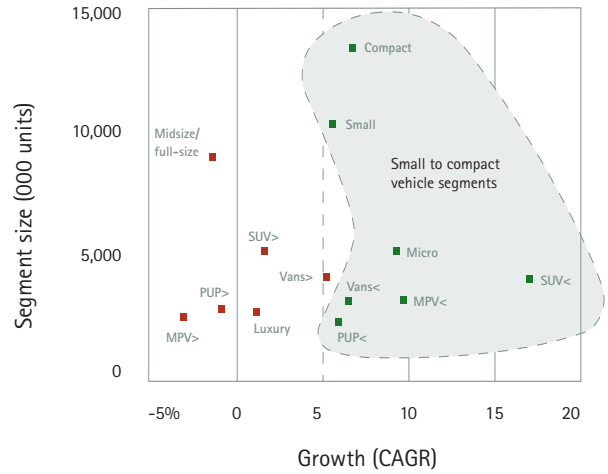
Smaller vehicles were driving the growth. Sales for larger cars were either stagnant or contracting.

Sales growth, indexed on 2003



\* Excludes heavy commercial vehicles and OEMs with fewer than 5,000 units in 2003. Source: Global Insight, September 2008; Accenture analysis

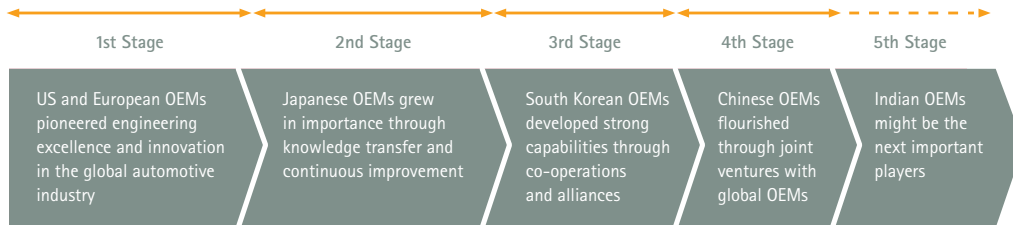
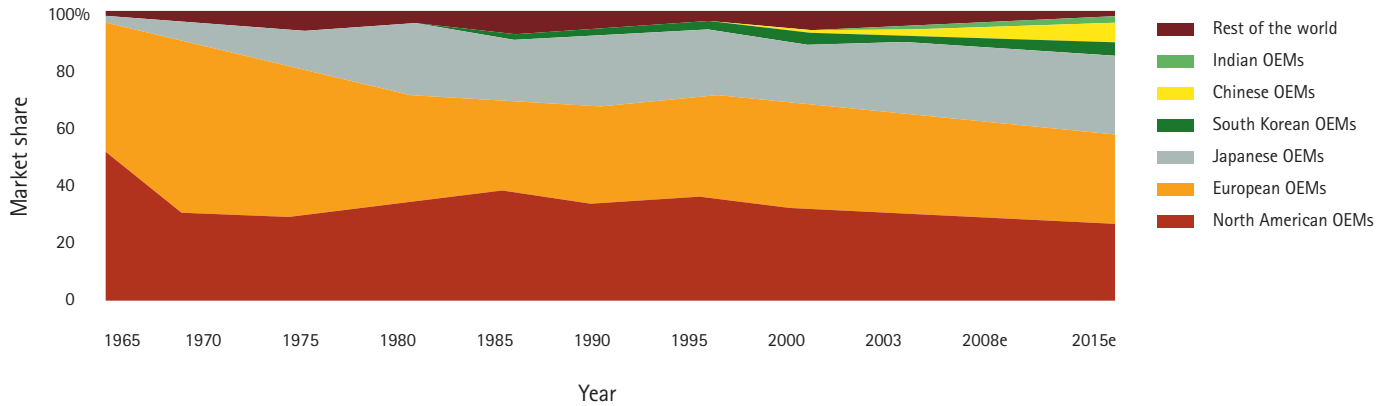
Segment size (2007) and growth (2003–2007)



SUV = sports utility vehicle; MPV = multi-purpose vehicle; PUP = pickup truck < = micro to compact; > = midsize/full-size to luxury Source: Global Insight, September 2008; Accenture analysis

We are now moving into the fifth stage for the global auto market, in which Indian, Chinese and South Korean OEMs are expected to capture a much larger share, while the shares of automakers in the Triad countries will fall.

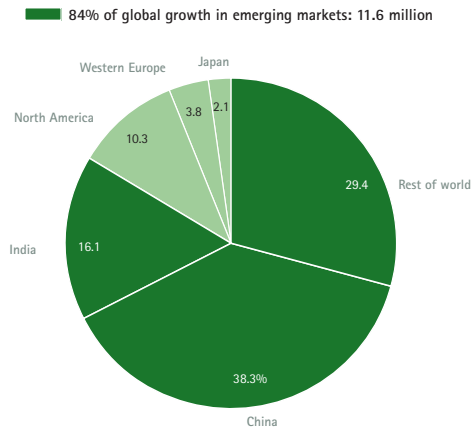
Vehicle production volumes, 1965–2015



Source: Ward's Automotive Yearbook; Global Insight; Accenture research

In fact, from 2006 until 2012, 84 percent of global growth is expected to come from emerging economies.

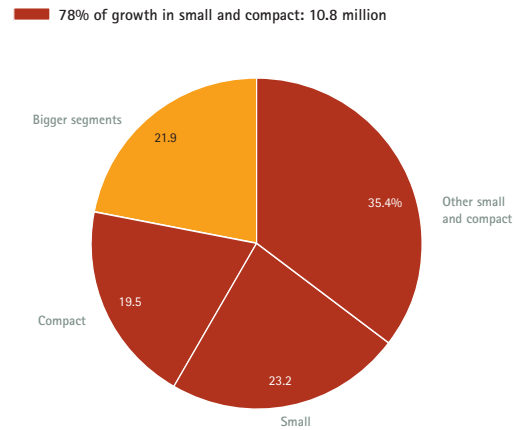
**Market growth forecast, 2006-2012**



Source: Global Insight, June 2007; Accenture analysis

Seventy-eight percent of growth in the global auto market from 2006 to 2012 is expected to come from small and compact vehicles.

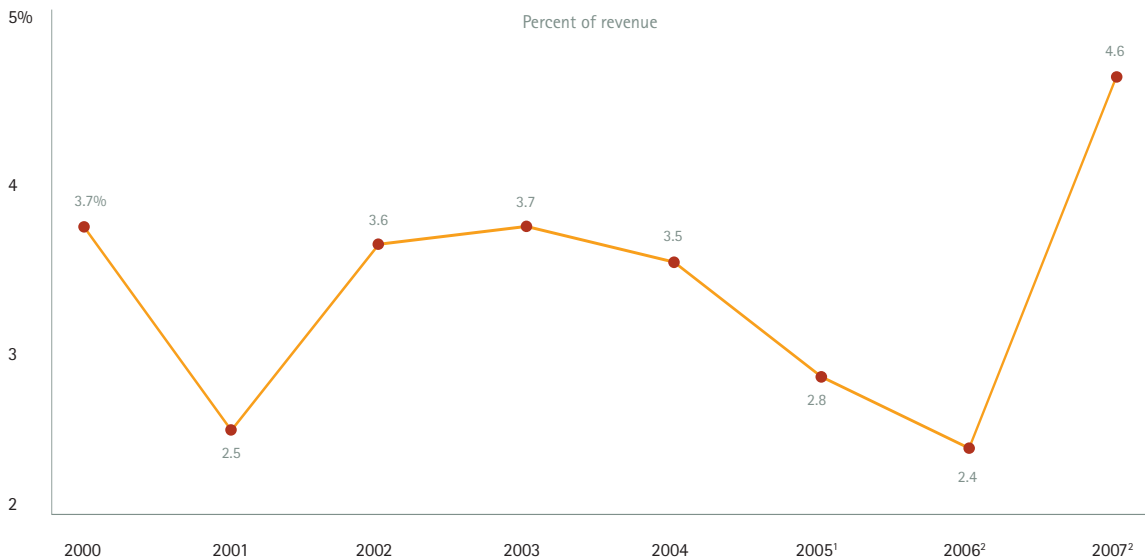
**Segment growth forecast, 2006-2012**



Source: Global Insight, June 2007; Accenture analysis

Although earnings before interest and taxes (EBIT) for the auto industry jumped to 4.6 percent in 2007, preliminary numbers for 2008 point to a sharp decline. For the first half of 2008, EBIT had already slumped to the 2006 level. Once figures for the second half of the year are in, we expect the 2008 number to be much lower.

**8-year EBIT margin of OEMs<sup>1</sup>, 2000-2007**



<sup>1</sup> Peer group includes the high-performance business peer set  
<sup>2</sup> Excluding Chrysler

Source: Onesource, 2008; Accenture analysis