



Industry Report | **Automotive**

Life in the fast lane

By John E. Cunningham, Umar Riaz and Eric J. Johnson

Automakers as a group have had limited success in creating shareholder value. There are remarkable exceptions, however—a small group of high performers that are much better at growing revenues than their competitors. In determining why, we have identified four key characteristics that are shared by the best companies in the industry.



■ Remember Hudson, Studebaker, Borgard and Leyland? Forty years ago, the world boasted more than 50 independent automakers. But slowing sales growth, overcapacity and product proliferation culminated in widespread industry consolidation in the 1980s and 1990s, and today, only a dozen or so economically independent companies are still in business.

The survivors are larger, having gobbled up weaker rivals to gain access to global markets. They are also leaner and more efficient, with broader product portfolios. Yet, despite the elimination of 250,000 jobs globally in the past decade and a 42 percent increase in productivity (in terms of revenues per employee), automakers as a group have had limited success in creating shareholder value.

To be sure, there have been some spectacular turnarounds, yielding dramatic near-term returns for investors. Operational improvements throughout the industry have led to better-quality vehicles, and product development time has been more than halved since the 1980s. But auto stocks in general remain extremely volatile, and the industry's shareholder returns lag the major stock market indices. High performance is an elusive goal for most automakers.

Not for all, however. Accenture defines a high performer in the auto industry as a company that has delivered outstanding and consistent total return to shareholders over a 16-year period (see "About the research," opposite). This represents a departure from our standard high-performance business methodology, which measures TRS over three-, five- and seven-year periods. But we believe it is justified

because of both the cyclical nature of the auto business and its very long product cycles.

In recent years, several carmakers have faced significant financial troubles—and then rebounded sharply. Typically, these manufacturers have ridden the success of one or more hot products but have then been unable to sustain that success through the inevitable downswings. For such companies, the shorter the time frame under investigation, the more distorted the results. By measuring a company's performance over a longer period as well as by looking at how consistent its performance has been, we can factor in the peak-to-trough cycles that make it so difficult to determine which companies really are genuine high performers, and which are merely boom-and-busters.

From our research emerged four companies that are clearly better able to sustain a positive return to shareholders over the long term and to produce more consistent annual positive shareholder performance than their peers. When we took a closer look at what sets them apart, we were in for some surprises.

Key drivers

It is not surprising that top-performing auto companies operate efficiently across the value chain—from product development through sourcing and manufacturing, to sales and marketing and after-sales service. They are among the industry's leaders in manufacturing productivity, product quality and product development cycle time.

But while it's undoubtedly true that operational excellence is necessary to achieve high performance, it does not

(Continued on page 14)

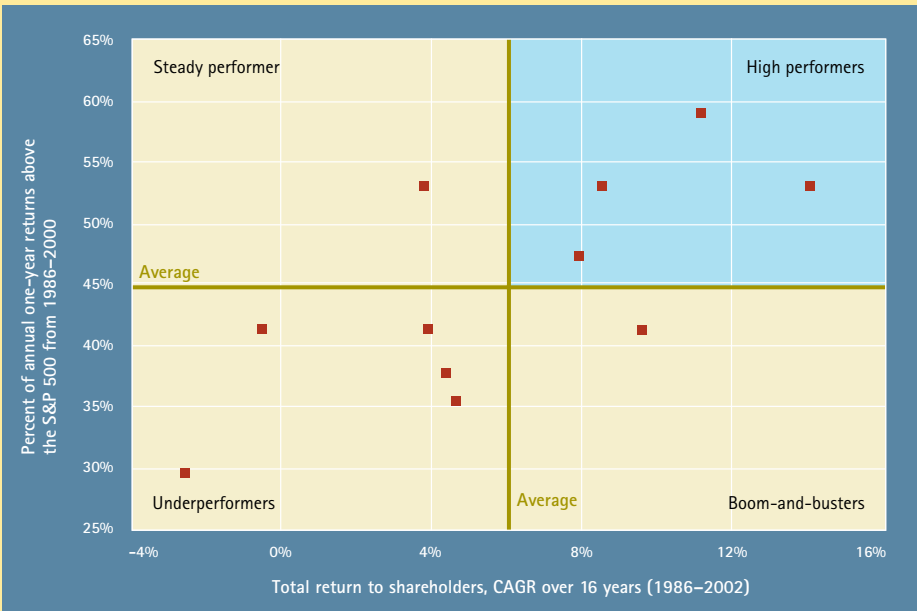
About the research

Accenture defines high performance in the auto business on the basis of two key dimensions: long-term shareholder performance and consistent shareholder performance. By applying an approach that emphasizes sustained and consistent positive shareholder returns over a longer term than the standard three, five and seven years, we were able to iron out the distortions caused by a few "boom-and-busters" (see story).

Long-term shareholder performance is measured as total return to shareholders (TRS) over the 16-year period from 1986 to 2002. This time period was chosen because of the industry's characteristically long product cycles. Consistent shareholder performance is based on the number of individual years between 1986 and 2002 in which an automaker's annual TRS exceeded the S&P 500 benchmark return. This dimension further captures an automaker's ability to produce relatively steady returns for its shareholders, in contrast to automakers that regularly undergo periods of decline followed by periods of recovery. Automakers that exceeded the peer averages on both the long-term and the consistency-performance dimensions were identified as "high performers."

Our shareholder return data covered the years 1986 through 2002—the period for which we were able to obtain share price and dividend data for all independent automakers (except Renault). We experienced a number of difficulties gathering comparable global data in other areas. For example, there is no standard productivity measure for automaker manufacturing and assembly plants outside North America. Because of such limitations, we were forced to rely heavily on US data; however, we believe that the US market mirrors global trends.

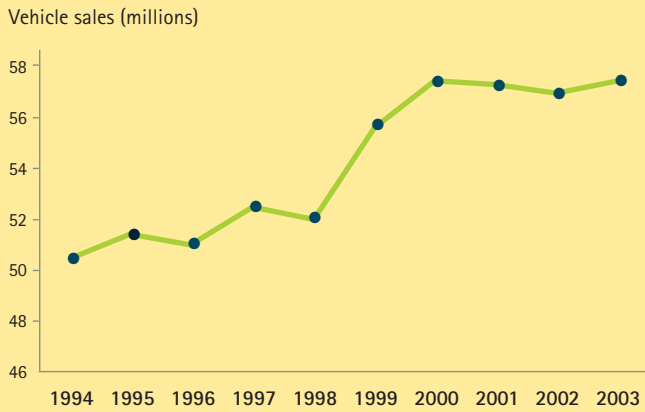
High-Performer Identification Framework



SOURCE: ACCENTURE ANALYSIS

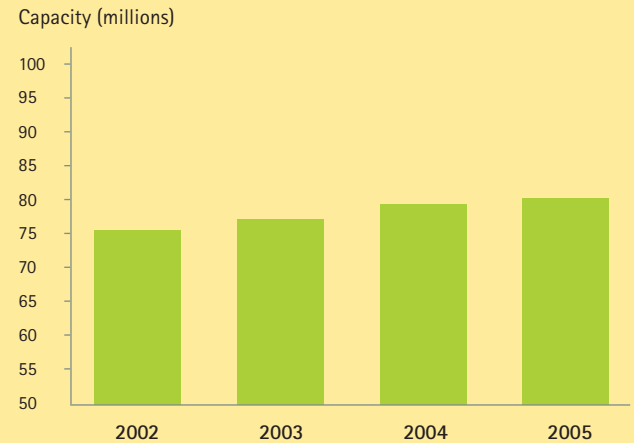
Challenging environment

Global vehicle sales growth is slowing . . .



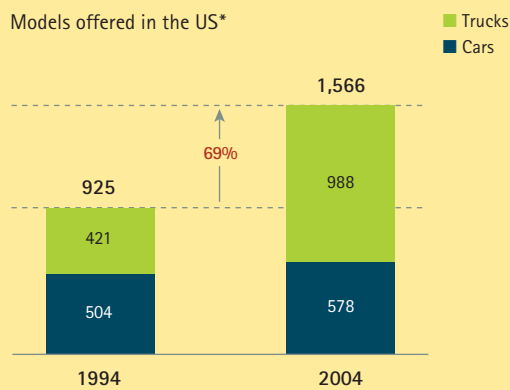
SOURCE: AUTOMOTIVE NEWS

. . . even as automakers add capacity . . .



SOURCE: ACCENTURE ANALYSIS

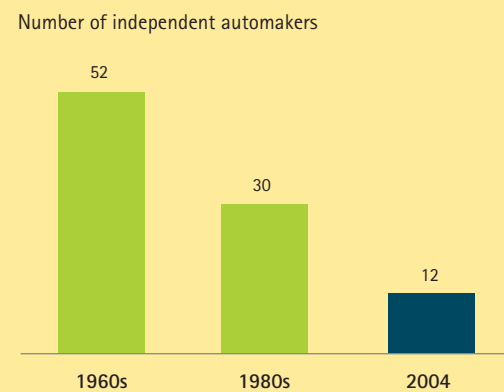
. . . and continue to launch more and more models.



*Models include major variations of nameplates (e.g., sedan/coupe, convertible, wagon)

SOURCE: MORGAN STANLEY, AUTOMOTIVE NEWS, ACCENTURE ANALYSIS

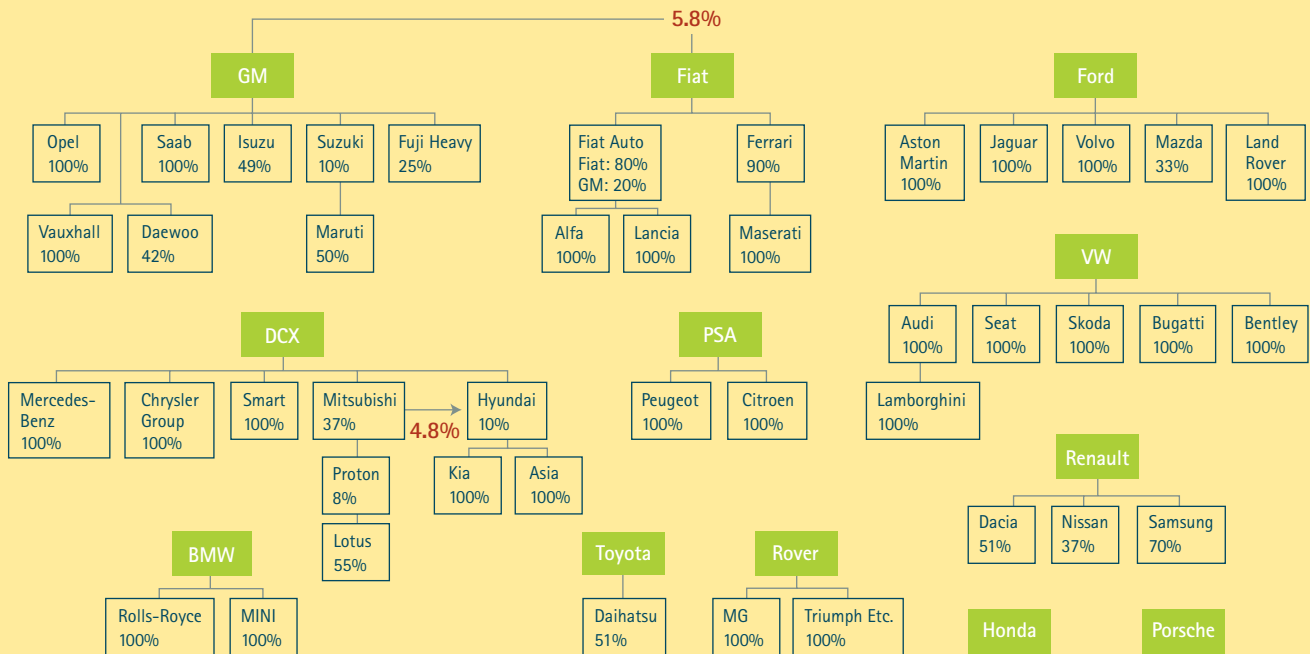
Automakers have responded with acquisitions . . .



SOURCE: DEUTSCHE BANK

... to increase scale, enlarge product portfolios and obtain access to global markets.

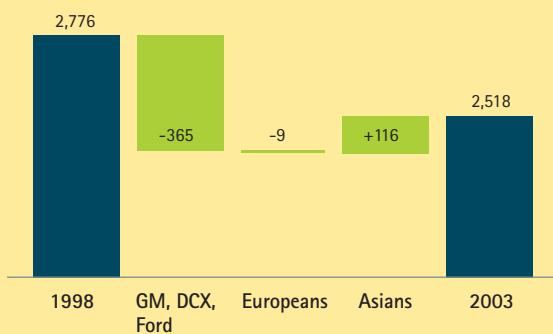
Automotive industry consolidation



SOURCE: DEUTSCHE BANK, ANNUAL REPORTS

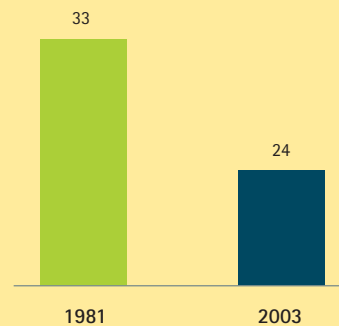
They have also become leaner . . .

OEM headcount (000s)

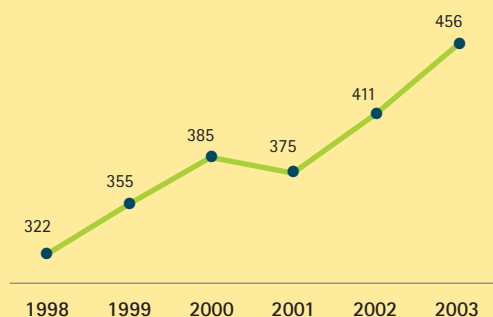


... and more efficient . . .

Productivity (assembly hours per vehicle)

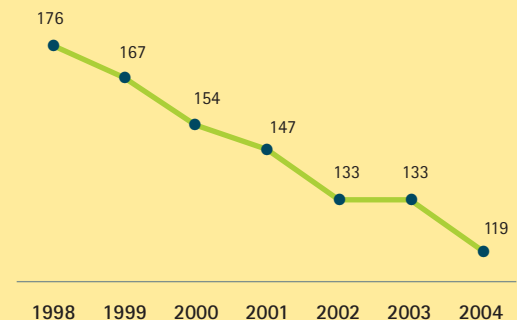


Revenue per employee (\$000s)



SOURCE: HOOVERS, ANNUAL REPORTS, ACCENTURE ANALYSIS

Quality (US, problems per 100 vehicles)



SOURCE: HARBOUR REPORTS, J.D. POWER

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guarantee it. What really distinguishes the top companies is something else.

In an industry with a very high fixed-cost structure, the ability to grow vehicle sales and revenues immediately translates into better operating margins as costs are spread across a larger base. All our high performers are much better at growing revenues than their competitors.

In determining why they are so much better, we have identified four key drivers or characteristics that are shared by all four high-performing automakers.

Organic growth

All our high performers have grown

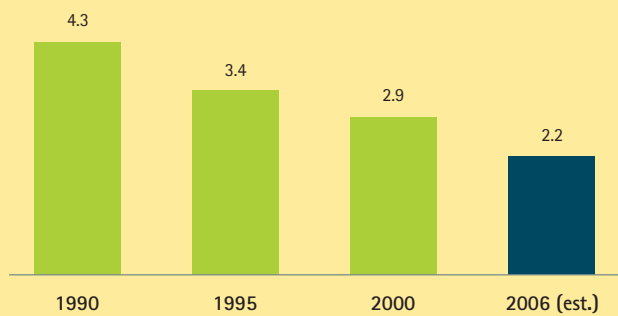
primarily through organic means, rather than as a result of mergers or acquisitions. Interestingly, since our list of high-performance automakers includes only one truly large-scale manufacturer, sheer size (the apparent goal of most merging and acquiring companies) doesn't seem to be of overriding importance in contributing to high performance in this industry—or, indeed, in any industry. (For a related article, see page 18.)

Simple, global brand portfolio

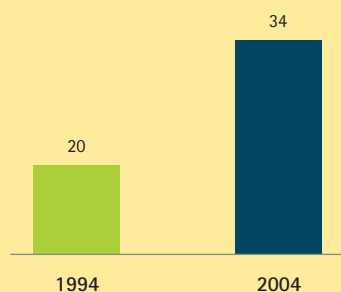
The sizable investment required to build and sustain a powerful brand must be leveraged globally. High performers excel in successfully exploiting one or two core brands and marketing them effectively worldwide. In contrast, many other automakers have a patchwork of

... with fresher product portfolios ...

Average showroom age (years, US market)



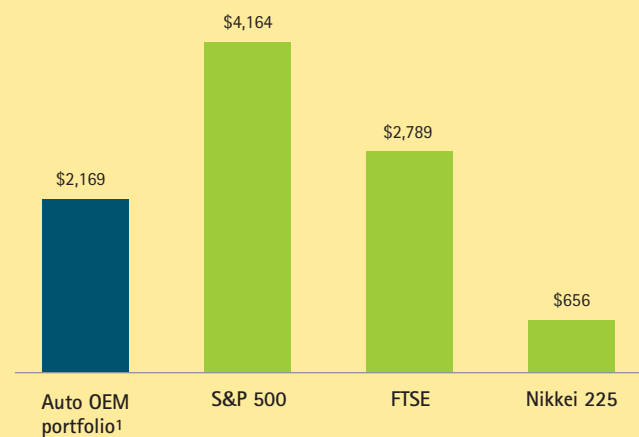
Average models per brand (mid-year, US market)



SOURCE: AUTOMOTIVE NEWS, MERRILL LYNCH, ACCENTURE ANALYSIS

... yet with limited success in improving shareholder performance.

Value of a \$1,000 investment, 1986–2002



¹ Result of \$1,000 invested in a market capitalization-weighted basket portfolio of GM, Ford, DCX, Honda, Toyota, Nissan, BMW, Fiat, Peugeot, Hyundai and VW.

SOURCE: ACCENTURE ANALYSIS

brands—some strong, some not—across different regions of the world.

Product innovation

Car buyers traditionally have a big appetite for the industry's newest products. High performers have newer model portfolios than most of the industry—an advantage that often translates into increased sales and share gains. By not necessarily competing in all product segments, high performers can focus on a few, higher-volume platforms and tailor their products to key customer areas. We believe this focus also boosts their ability to quickly innovate and rapidly develop new models.

Sales and marketing

The automotive industry has gone through several cycles in the past few decades. Before the 1980s, companies competed on the basis of size and corporate structure, and the bigger companies dominated. In the 1980s, led by the Japanese, automakers woke up to the manufacturing realities of productivity and quality, which caused them to invest in manufacturing and quality upgrades. In the 1990s, they focused on product proliferation as the primary means of competition, and most of them broadened their product scope.

By combining a focus on a core set of global brands with younger product portfolios, high performers have successfully avoided offering consumers the high levels of incentives that have plagued many of their competitors. Even with lower incentives—often worth thousands of dollars per unit to a company—high performers have consistently outsold other automakers.

Emerging trends

Today, the competitive landscape in this industry is changing yet

again. Accenture strongly believes that sales and marketing will be the critical determinants of high performance over the next decade. There are several trends making these areas important.

Convergence of operational capabilities

The differences in key metrics such as manufacturing productivity, quality and product development times are converging to such an extent that high performers sometimes hold only a minor advantage. We believe this convergence will continue.

Increased product proliferation

Through the use of global platforms, flexible manufacturing and shorter product development times, companies will bring an increasing number of products to market, faster.

Shifting brand landscape

Traditional luxury brands are entering the market at lower price points. Mass-market brands are increasingly offering more expensive vehicles. Performance brands are offering family vehicles, and family brands are moving the other way. We believe that this blurring of boundaries between brands will increase in the future.

To win in the new era of sales and marketing, automakers will need to assemble a clear and integrated set of capabilities.

Like other consumer product companies, automakers will require a superior management structure that integrates decision making across all key functions—production, marketing, sales and the retail network. They will also need to leverage the very latest in marketing analytics and know-how to guide their decision making. Only by bringing together vehicle and customer insight will they be able

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Honda: Why small is smart

Honda Motor Co. is the youngest of the world's major automakers. It is also fiercely independent. Indeed, the company's management firmly believes that independence is critical to quick decision making—and, therefore, essential to success in the ever-changing auto business.

The company exhibits most of the capabilities essential to high performance—and in some, it's well ahead of the game. Take product development.

Honda is well known in the industry for its flexible and global manufacturing system, nicknamed "Ultimate Flex." While other automakers have boosted productivity by dedicating each plant to a single model line, Honda retrofitted its plants so that each one could build nearly every car in its lineup. The upshot: improved efficiency, improved response to changing market demands and the ability to profitably market a more diverse product lineup.

It's a similar story with the company's marketing philosophy, which emphasizes staying close to its core customers. Honda has grown organically and has moved into new product segments as its customers' lives and needs have evolved. As a result, the automaker enjoys lower marketing costs per vehicle and better price realization.

Both marketers and engineers frequently participate in ethnographic research to gain an insider's point of view by actively observing customers using products in a natural environment. In developing the Honda Element SUV, for instance, senior corporate executives spent months observing, talking to and experiencing the lives of their targeted market segment— young, active males.

Honda has also elected to focus on just one global brand— Honda. The Honda brand is focused on volume markets and conveys images of superior quality, coupled with youthful appeal. Acura, a North America-only brand, by contrast, concentrates on the luxury market. Significantly, in view of the Chinese market's potential, China accounted for 17 percent of Honda's total net income in the third quarter of last year.

to deliver the right vehicles to the right customers, via dealerships equipped to serve them.

Technology and data management underpin all these process capabilities. High-speed data access and processing, user-friendly analytical and data visualization tools, sophisticated modeling and simulation tools—all will be essential components of a highly coordinated data processing system to ensure the requisite customer and vehicle insight. All, moreover, will need to be aligned with both strategies and capabilities if a high-performing sales and marketing organization is to result.

Of course, while sales and marketing will be the hallmark of the next decade, operational excellence will remain a critical requirement. Automakers must achieve and sustain competitive levels of quality, productivity and cost efficiencies across the value chain to finance

the increased investment necessary to develop the sales and marketing capabilities that will lead to high performance.

In addition, high-performing auto companies will have to deal with a couple of wild cards.

Environmental challenges

The pace at which "green" technologies are legislated, developed and implemented will have a profound impact on the relative competitive positioning of car companies in the future.

Emerging markets

Light-vehicle sales in emerging markets are expected to grow 10 percent a year through 2009, with China leading the way. Moreover, China and India might well become export markets, disrupting the competitive dynamics of the developed markets. Car companies already have begun to pour investment dollars into China. How the Chinese

BMW: Fast and flexible

Munich-based Bayerische Motoren Werke is no ordinary German company. In a country where notoriously rigid labor laws might be expected to compromise performance, BMW is, in fact, incredibly responsive to customer needs and demand while maintaining enviable levels of efficiency and productivity.

The key to BMW's success? Flexible shifts that allow the automaker to operate its plants at close to full capacity. If employees work more than their union-negotiated 35-hour week, they "bank" the extra hours. If demand drops, they can withdraw time from the account and take days off; most get long weekends in exchange for working some Saturdays.

This flexibility is not confined to labor relations. All BMW plants can produce at least two different models, so when demand surges for a particular model, the company can add capacity where it needs.

It all helps when it comes to servicing BMW's customers, many of whom are far from flexible. Indeed, European customers—80 percent of whom custom design their own cars—can be extremely demanding. Because customer focus is central to BMW's business, the automaker offers its customers the opportunity to change every detail on the car until five days before production; this is made possible by software that can handle each month up to 120,000 customers who change their minds about just what sort of car they want.

Like Honda, BMW has expanded organically. It bought the UK's MG Rover Group in 1994—only to turn around and sell it in 2000 to, as the board of management said at the time, "grow under its own power... extending [the BMW brand] all the way to the luxury performance segment."

By focusing on a small set of brands—BMW, MINI and Rolls-Royce—and supporting each brand with a simple, consistent and global image, BMW has been able to move successfully into segments like SUVs and subcompacts.

and Indian markets develop, as well as how quickly they develop, will have a tremendous impact on the auto business.

The next decade promises to be yet another interesting chapter in the history of the industry. Will the high performers of the past manage to sustain their position in the face of more consolidated, operationally more capable competitors? That depends on which companies win the burgeoning sales and marketing war for the hearts and wallets of automotive consumers, and on which ones capitalize on green technologies and the growth of emerging markets. ■

About the authors

John E. Cunningham is the managing partner of the Accenture Automotive industry group. Previously, he oversaw all of the company's North American automotive and industrial operations, and he managed Accenture's overall relationships with its largest automo-

tive OEM clients. Mr. Cunningham has extensive experience in the industry: He helped develop supply chain strategies and implement financial management processes for automotive manufacturers; he has managed the development of numerous IT strategies for automotive and industrial clients; and he has worked with many startups that provide various automotive solutions. Mr. Cunningham, who is the managing partner of Accenture's Detroit office, is a member of the University of Michigan Business School's Alumni Board of Governors.

john.e.cunningham@accenture.com

Umar Riaz is a partner in the Accenture Automotive industry group. Based in New York, he consults on a wide range of topics, including corporate strategy, sales and marketing, product development and operations. Before joining Accenture, Dr. Riaz worked in product strategies at Ford Motor Company. Dr. Riaz, a post-doctoral fellow at Harvard University,

holds three US patents in the area of materials science.

umar.riaz@accenture.com

Eric J. Johnson is a senior manager in the Accenture Strategy & Business Architecture service line within the company's Automotive industry group. For more than 11 years, he has been formulating sales and marketing strategies, performing quantitative financial analysis and working in CRM. Mr. Johnson, who is based in Chicago, has recently headed a strategy engagement with a leading US automaker's sales and marketing organization.

eric.j.johnson@accenture.com