Car Dealer Sentiment: OEMs Need to Act Now to Prevent Margin Loss

BCG Study Reveals Greater Need for Analytics and Management of CO_2 Penalties

By Jonas Anselm Stein, Dr. Andrej Levin, Alfred Wiederer, Dr.-Ing. Peter Wiedenhoff, Dr. David Langkamp, and Dr. Mario Farsky

The disconnect between sales motivations for German auto dealers and the need to slash fleetwide CO_2 emissions could cost automakers billions of euros in annual fines.

As the recession created by the Covid-19 pandemic accelerates a downward price trend in the German auto market, dealers and automakers have the opportunity to align their goals better to weather the storm and safeguard profits..

In a recent survey, Boston Consulting Group (BCG) talked to more than 430 German auto dealers in order to compile a database of facts about dealer pricing and how dealers handle requirements to sell vehicles that produce fewer CO_2 emissions. Two main findings stand out:

- There is a deep disconnect between dealers' sales motivations and the need for automakers to slash CO_2 emissions fleetwide to avoid billions of euros in annual fines.
- Dealers too often leave money on the table by relying on gut feeling rather than analytics to manage incentives and discounts.

Despite facing common price and margin pressures, dealers and original equipment manufacturers (OEMs) sometimes work at cross-purposes and need to find ways to align the areas where they are out of sync. With 60% of auto dealers—65% for premium brands—expecting car prices to fall for the remainder of the year, the recession is actually an inducement for the industry to tackle these issues collaboratively. As they work to maintain sales, automakers need to avoid the last recession's responses by controlling discounts and avoiding price wars.

For its research, BCG talked to dealers from a range of brands selling a broad lineup of internal-combustion and alternative-powertrain vehicles. The interviews were conducted in May and June. BCG asked which promotions have the most significant impact on the purchase of new cars and electric vehicles (EVs). The survey also asked dealers whether they use analytics to guide discounts and incentive offers. It sought to identify the level of OEM support for dealers, discover the dealers' knowledge of penalties for CO_2 emissions, and determine their preparedness to change business practices and marketing to foster green-vehicle sales.

HOW MANY SUBSIDIES ARE ENOUGH?

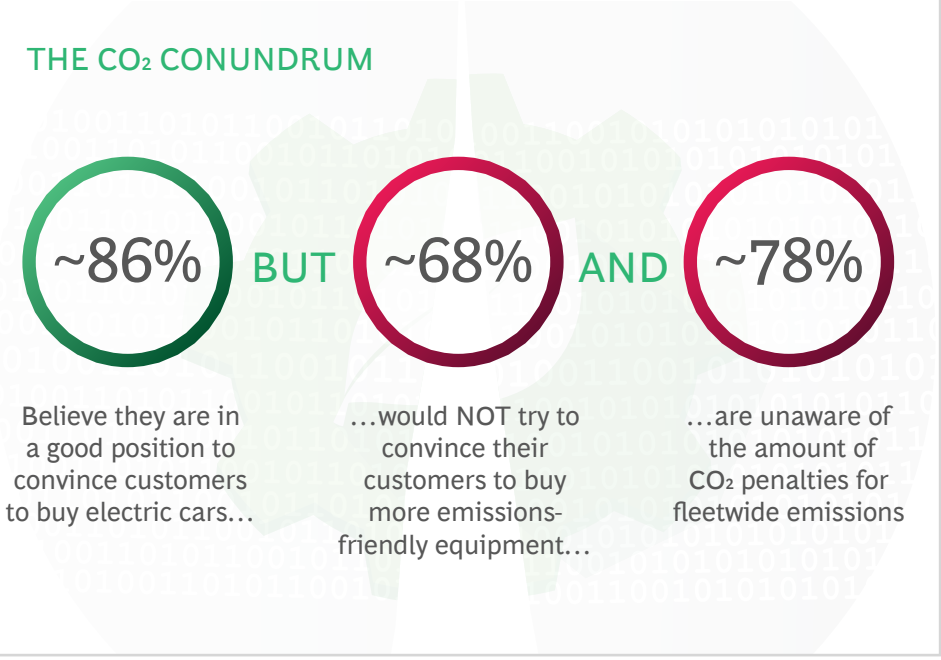
Germany has a complex incentive-and-tax program to speed the adoption of EVs. Consumers can get up to €6,000 from the government, depending on the car value. Dealers responding to the survey said they believe the government overspends. They say a €4,600 discount is big enough to sell EVs. The market for hybrids and EVs is growing quickly: First-quarter sales of battery-electric and plug-in hybrid vehicles rose 225% from the same period a year ago, even as total car registrations fell 20%. However, delivery times of six months or more are not uncommon, and several models are currently not even available.

The CO_2 Conundrum

Dealers responding to the survey expressed support for, and are bullish on, EV sales, saying the technology will transform the industry. That is especially true of those selling premium brands: 86% say they are qualified to pitch sales of EVs.

Yet dealers report a low propensity for steering customers to lower-emission car choices. With the new Worldwide Harmonized Light Vehicle Test Procedure (WLTP) norm in effect, those choices include auto options that affect emissions. CO_2 levels are influenced not just by the engine or hybrid drivetrains, but also by options such as wheel size and type. In fact, 68% of the dealers say they would not try to switch a customer's preference to a vehicle with lower CO_2 emissions. And dealers don't fully understand how their actions might decrease automaker profits by contributing to fleetwide environmental fines. A full 78% of the dealers are unfamiliar with the CO_2 penalties facing the OEMs. (See Exhibit 1.)

Exhibit 1 |



There are multiple reasons for this disconnect. Even without eco-discounts, the world of dealer and OEM incentives is complex. Automakers typically offer dealers incentives that are based on the volume of vehicles sold, total revenue, or other performance metrics. Although both dealers and OEMs strive to maximize sales volumes, automakers must also balance their fleet emissions and margins. Stricter European Union CO_2 penalties requiring automakers to keep an even more watchful eye on their sales mix start in 2021. Average CO_2 emissions for all the vehicles an OEM sells annually cannot exceed a threshold value. If they do, every additional gram of CO_2 will cost €95 per car sold. That has the potential for enormous economic harm. Various industry estimates calculate that penalties would range from

€10 billion to €20 billion next year, depending on how successfully OEMs manage to switch consumers to lower-emission vehicles. As Europe's largest auto market, Germany plays a vital role in reducing emissions.

Automakers need to help educate dealers on how to use eco-discounts to create the most optimal sales mix. Dealers need to know more about the emissions-friendly recommendations they can give to their customers. Almost half of dealers said they lack the information to do so. Yet they are open to using the discounts to help OEMs lower the carbon footprint of vehicles sold. OEMs should adjust dealer rewards to encourage the sales of vehicles that are less carbon intense in order to lower their CO_2 penalty.

The Incentives Game

More than 85% of the dealer respondents said they rely on their personal experiences, or "gut feeling," to select what they consider to be the best promotion mechanism. Only 19% tap into sophisticated automaker analytics to judge how to offer discounts and incentives. Only 34% maintain in-house analytics capability. With razor-thin margins, the industry can't ignore any profit sources. This lack of scientific application to creating a promotion program likely results in poorly optimized discounting strategies. Dealers can give discounts that are too high and cut margins, or they can be too stingy with discounts and lose business. They need a much more targeted, data-driven approach.

Dealers typically consider cash to be the best incentive to stimulate purchases, modulating what they offer on a trade-in or mentioning eco-discounts. They miss out on the wider use of nonmonetary incentives, such as providing an extended warranty, free service, or tossing in options when the customer orders the vehicle. Dealers may be confused by the different programs offered by OEMs.

One dealer told BCG, "Customers that are at all coming to the dealership these days are telling us that the purchase depends on a cash rebate."

Automakers and dealers should professionalize rebate management and strengthen the role of analytics so that they can select the right discount mechanism for customers.

WHAT SHOULD ANALYTICS FOCUS ON?

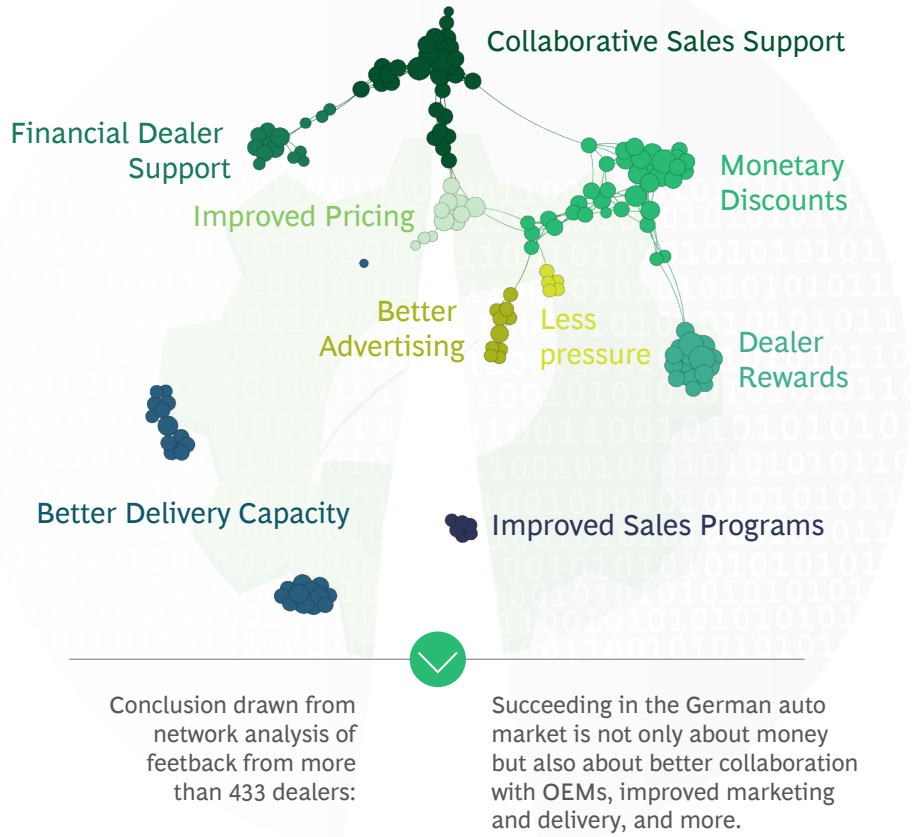
Analytics have the largest potential to raise margins by improving the understanding of customer price elasticity. OEMs currently give rebates on aggregated segments and on broad national campaigns. Automakers have a significant opportunity to more finely target customer segments and more smartly distribute rebates in areas where the investment would make a difference, while reducing rebates on segments with low elasticity. Given the complexity of robust analytical elasticity models on microsegments, OEMs need to support their dealers

.Actually Working Together

Dealers are looking for more help from automakers to support sales efforts. They are asking for clearer, less complicated sales and promotion programs, including longer warranties. One dealer told BCG that a five-year warranty would give the brand a positive image and demonstrate that the automaker trusts its products. Dealers said OEMs should present a more comprehensive array of leasing and financing offers to better meet customers' needs. Unlike the US and other regions that carry inventory from which consumers can select, the German car market is mainly characterized by a build-to-order approach. Dealers are also pushing for an improved process that includes more updates and transparency on vehicle delivery dates to keep customers informed. (See Exhibit 2.)

EXHIBIT 2 |

OEM support for dealers should be more than monetary



Conclusion drawn from network analysis of feetback from more than 433 dealers:

Succeeding in the German auto market is not only about money but also about better collaboration with OEMs, improved marketing and delivery, and more.

“We want collaborative ways of working with dealers—not business as usual,” one dealer told BCG.

Although the following requests from dealers might sound like a well-known and expensive wish list to most OEMs, they constitute four key actions that automakers and dealers can quickly collaborate on to improve income.

- Avoid long-term erosion of profit margins through aggressive, untargeted discounting.
- Professionalize rebate management so as not to leave money on the table. Dealers should make greater use of OEM-generated analytics to better match discounts with buyers. And automakers need to provide dealers with easier, action-oriented analytics to incorporate into their sales efforts.
- Close the communication gap between automakers and dealers by providing greater transparency on deliveries and more training on eco-discounts and other programs.
- Help dealers navigate the auto market as it changes because of environmental concerns and the greater use of digital tools. OEMs should provide dealers with more information for pitching the next-best lower-emission car choice to consumers.

Dealers are looking for closer collaboration, and there are plenty of areas where both sides can work together. There’s room, for example, to leverage analytics to garner the most impact from promotions. And they can work to push emissions incentives in ways that channel customers to greener alternatives and thus reduce penalties.

With billions of euros invested in promotions, and significant CO_2 fines on the horizon, it’s time to build a new, data-driven, strategic collaboration model.

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Also see one of our latest publications "How to Avoid the Auto Industry's Looming Price War"
https://www.bcg.com/publications/2020/avoid-auto-industry-price-war.aspx

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