KPMG
cutting through complexity

Global Automotive Retail Market

From selling cars on the spot to centrally managing the retail grid

September 2013

Part II

II Automotive retail market maturity model

Explanation | expert opinions

Explanation of KPMG's retail market maturity model

During its maturity process, each automotive retail market goes through an easy selling and hard selling period (shown in the graph on the 'Generic maturity process of automotive retail markets').

Both periods involve completely different retail strategies, dealer business models, sales staff competencies, management styles and KPIs. These differences have a major impact on the development of the retail network structures in each market.

In an easy selling period (where demand for new cars is high), a decentralized network evolves, with many retail outlets to generate high sales volumes and win market share (as shown in the first quadrant). At this stage, it is not possible to centralize and move into the fourth quadrant. As soon as new car demand cools down (as the market enters the hard selling phase), decentralization becomes wasteful, with the cost of maintaining so many outlets reducing dealer margins – as illustrated in the second quadrant.

At a certain point in a market's maturity, the only way to be consistently competitive is to steadily consolidate and centralize the retail network, to reach the key third quadrant.

Structure should follow strategy, but retail strategies change over time

For the global auto retail sector, the common principle of 'structure following strategy' needs to be redefined. Typical network planning horizons are limited to 5 years; these should be extended to 10-15 years, in order to prepare for the challenges of increasing maturity and the change from easy to hard selling.

Most companies' retail strategies in establishing markets focus on generating sales volumes solely through customer acquisition only. Once the era of easy selling comes to an end, retail networks may struggle to maintain margins, as sales decline.

As soon as a market's demand for replacement cars exceeds the demand for first-time purchases (heralding the arrival of the hard selling period), the retail emphasis needs to change from customer acquisition to loyalty and retention. This shift should be reflected in network planning and requires greater centralization, to gather and process the vast amount of data needed to effectively manage customer relationships.

Prof. Dr. Willi Diez
Director,
Institut für Automobilwirtschaft (IfA)

Centralization needs to be redefined to create an efficient retail grid

Our interviews with key industry decision-makers revealed some of the challenges in designing an optimal retail network.

It is widely acknowledged that too many decentralized PoS create overheads and intra-brand competition, which eats into dealer profits in a hard selling environment.

Yet simply reducing the number of PoS – by setting up centralized superstores – brings other problems, such as lack of local knowledge and relationships.

Auto retailer groups should not be considering whether to centralize; they should instead be assessing how to manage a centralized retail grid. The question remains whether this management should be the responsibility of OEMS, dealer groups or even third parties.

Dieter Becker
Partner, KPMG in Germany
Leader of KPMG's
Automotive Think Tank

"Centralization cannot be the solution for all our retail problems – we will always have to live with a certain degree of waste to be able to cater to all our customers."

Managing Director,
OEM-owned (captive) retail group,
Western Europe

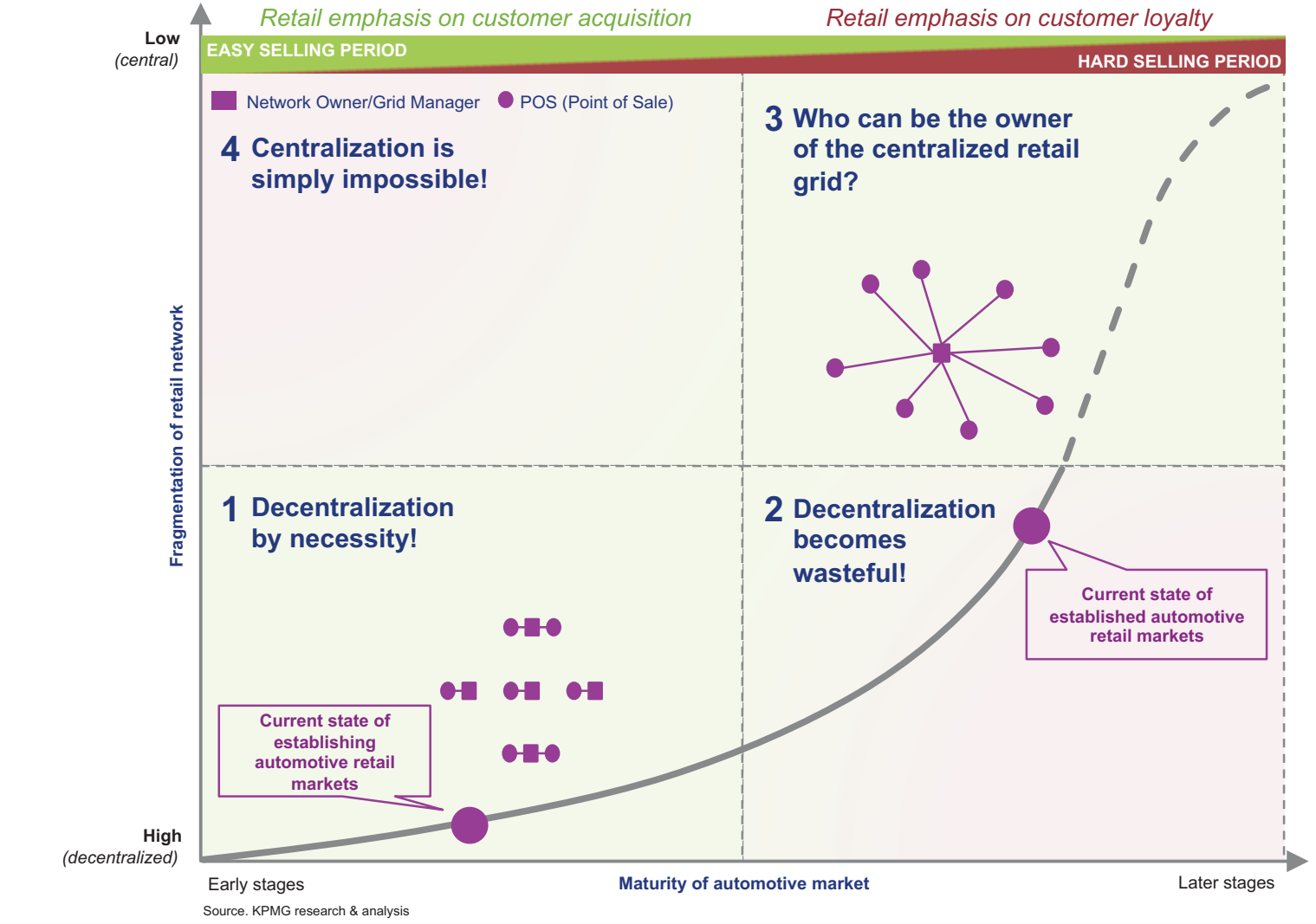
"Having too many points of sale is poison for our retail network's profitability; they simply create too much overhead and intra-brand competition."

Director,
Retail Network Development,
Premium OEM, Western Europe

"We will increase the number of dealers by at least a hundred per year until 2016 – and even beyond if the demand remains high."

Senior Director,
Network development,
European-Chinese joint venture

Automotive retail market maturity model
Generic maturity process of automotive retail markets



Source. KPMG research & analysis

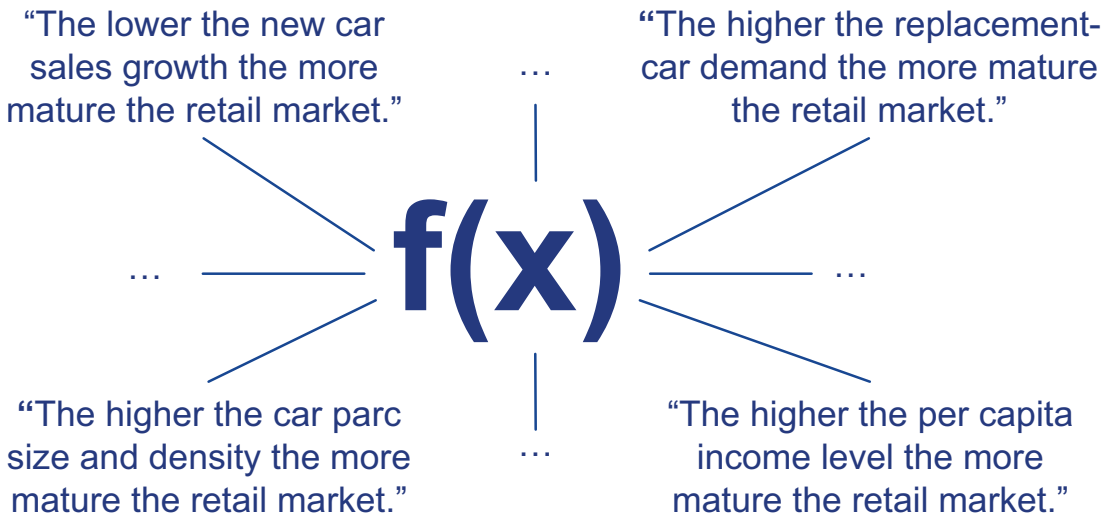
Our research shows that every automotive retail market passes through certain stages of maturity.

In the initial, easy selling period, demand for new cars is high, with minimal distribution problems or risks. At this point, retailers are focused on providing sufficient cars to keep up with customer needs, which leads to fast growth of outlets and a decentralized, fragmented structure.

As demand for new cars eventually slows, competition increases and the market reaches the hard selling phase. As new car profits decrease and customers become more sophisticated, the retail network is steadily consolidated to reduce operational costs.

Expert view on a retail market's maturity process

"The automotive retail market maturity level is a function of a variety of market-specific features and macroeconomic conditions."



Many factors that determine a market's maturity level can be easily observed

A first indicator of a market's maturity level is the contribution of new car sales to the overall automotive retail value creation. In mature markets, the demand by first-time buyers tends to be considerably lower than for replacement cars. This leads to lower annual growth rates, as purchasers of replacement vehicles are more likely to postpone their decision.

Another guide is the car parc size, which heavily increases during the road to maturity, before reaching saturation point.

The combination of car parc and population size is another revealing barometer. In the mature markets of North America, Western Europe and Japan, vehicle ownership rates have reached well above 50 percent (as in Japan, France and Germany) and close to 100 percent in the US.

Prof. Dr. Willi Diez
Director,
Institut für Automobilwirtschaft (IfA)

Automotive retail market maturity model
What makes a retail market mature?

Market features / *Market status*	Mature markets	Establishing markets
New car sales	■ new car sales are often stable or even declining in year-on-year ■ replacement car demand comfortably exceeds demand for first cars	■ new car sales growth rate over the last 10 years is often double digit ■ first car demand considerably exceeds replacement-car demand
Used car sales	■ used:new car sales ratio is between 1:1 and 3:1	■ used:new car sales ratio is often below 1:1, depending on the new car sales growth
Car parc density	■ vehicle ownership rate is usually above 50 percent	■ vehicle ownership rate is usually below 50 percent
Income level	■ average annual disposable income per capita (of the driving population) is well above 30,000 US Dollars (US$)	■ average disposable income per capita (of the driving population) is below US$20,000
After-market and service culture	■ original equipment supplier (OES) market share is often above 30 percent	■ due to a high proportion of drivers carrying out repairs themselves ('do-it-yourself' – DIY), the independent after–market is dominating the OES sector
Finance and insurance	■ over 90 percent of all vehicle purchases are financed	■ most car buyers pay for their vehicles in cash
Mobility-as-a-service (MaaS)	■ demand for individual mobility is steadily decreasing	■ strong demand for individual mobility, as one's own car is an important status symbol
Urbanization level	■ the urban population often comprises more than 80 percent of the total population	■ urban population is often below 60 percent of the total population
Retail network structure	■ a high proportion of authorized/franchised dealers ■ an organized commercial used car market	■ low share of authorized/franchised dealers ■ unorganized (mostly private) used car market
Retail network density	■ the total number of dealerships is constantly decreasing, due to competition and low profits.	■ the number of dealerships is constantly rising to satisfy steadily increasing demand.

Source: KPMG research & analysis.

The maturity of an auto retail market depends on a variety of features and macroeconomic conditions, which influence evolution of the structure and determine the speed of maturity.

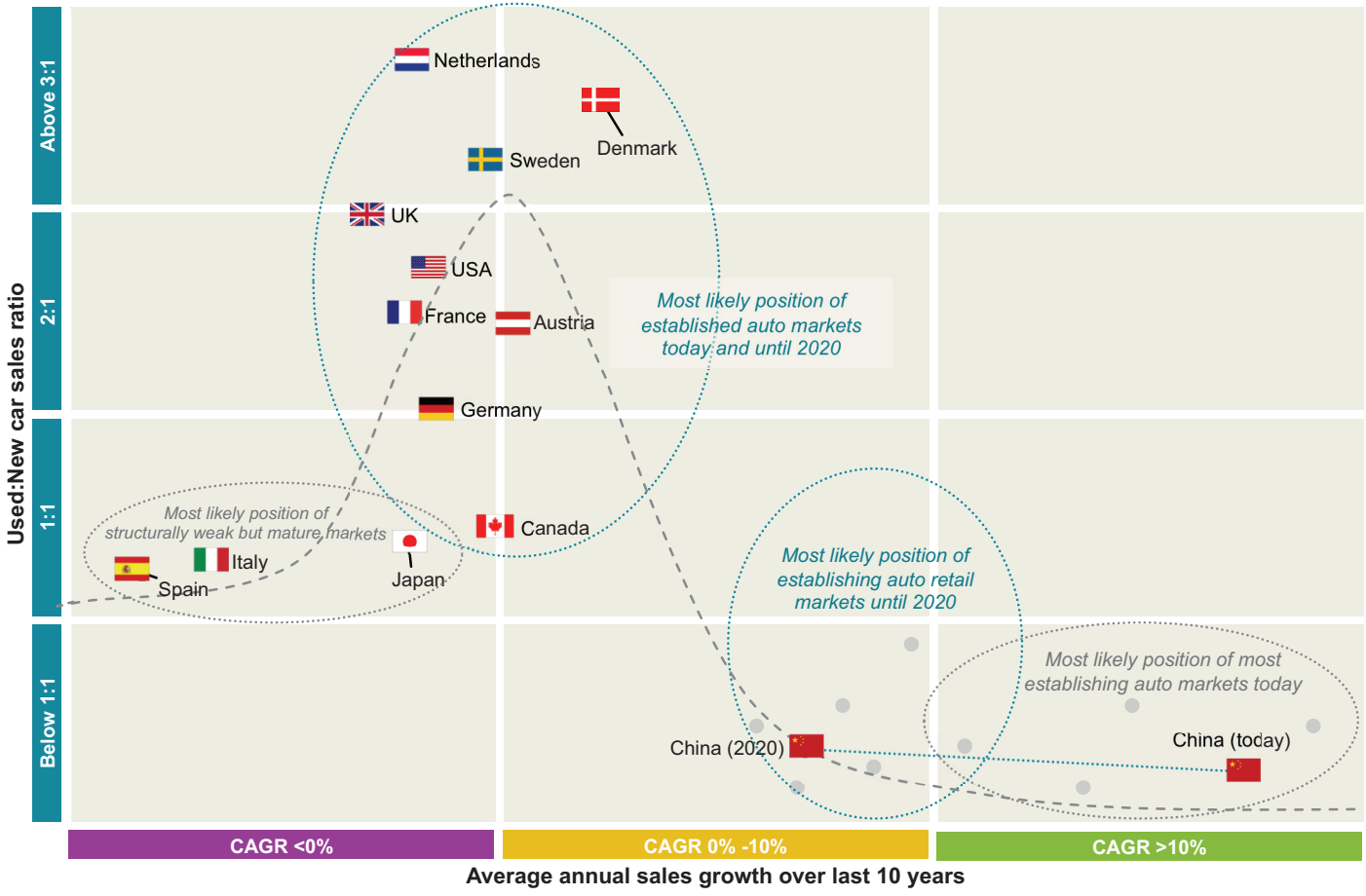
Establishing markets such as China will reach higher levels of market maturity quicker than existing established markets.

By 2020, none of the establishing markets – such as China, India and Brazil – will have reached a degree of maturity comparable to current levels in North America, Western Europe or Japan.

Nevertheless, the level of maturity can also differ within a single market. One example is China, where the market maturity in urban centers like Shanghai or Beijing is certainly higher than in the lower tier cities and rural areas.

Automotive retail market maturity model
Maturity level analysis | new and used car sales

New car sales growth and used:new car ratio indicate a market's maturity level



Source: KPMG research & analysis, LMC, Euromonitor, BCA, National Trade Bodies.

Key takeaways

To assess the current state of the most important auto markets, we have analyzed new car sales growth over the last 10 years, along with average used:new car ratios.

Reliable and comparable information on used car market volumes and trends is only available for a very limited number of markets. Our research suggests that new car sales typically lag behind used car sales in most established markets, while in establishing markets, the opposite is true.

In established markets, every new car sale is matched by 1-3 used car sales, while in China the ratio is around 1:5 in favor of new car sales.

Even by 2020, the used:new car ratio in China will not reach the levels currently seen in established markets. Beyond 2020, China will be expected to slowly follow the dotted line to a higher level of maturity.

The BRIC markets will make great leaps until 2020, but will still lag significantly behind

Source: KPMG research & analysis, LMC, Economist Intelligence Unit (EIU).

Key takeaways

The comparison of car ownership rates and income levels provides a further indication of the different levels of market maturity around the world.

With the exception of the US, Australia, Norway and Switzerland, all established auto markets are very close to each other, with per capita income well above US $20,000 and a vehicle ownership rate of more than 50 percent.

All BRIC markets have an ownership rate below 50 percent, with Russia alone predicted to come close to 50 percent by 2020.

Although China is forecast to make a big leap between 2013 and 2020, its income level and vehicle ownership rate will still lag behind many other establishing auto markets for the foreseeable future.

India's low income levels means that it will not even come close to market maturity by 2020.

Automotive retail market maturity model
Maturity level analysis | car and population density

Population density can be a limiting factor on the road to maturity

Source: KPMG research & analysis, LMC, World Bank.

Key takeaways

Population density can have varying impacts on maturity, depending upon other social, economic and geographic conditions.

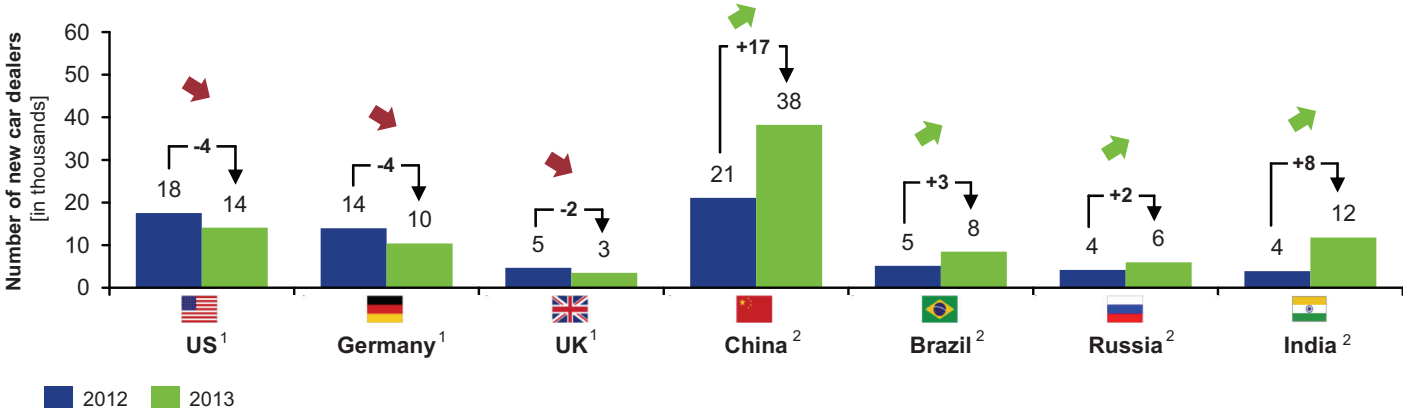
For example, India's population density is already as high as Japan and Belgium, and will continue to increase in the next 7 years.

However, India's social, spatial and environmental restrictions will restrict the growth in car ownership.

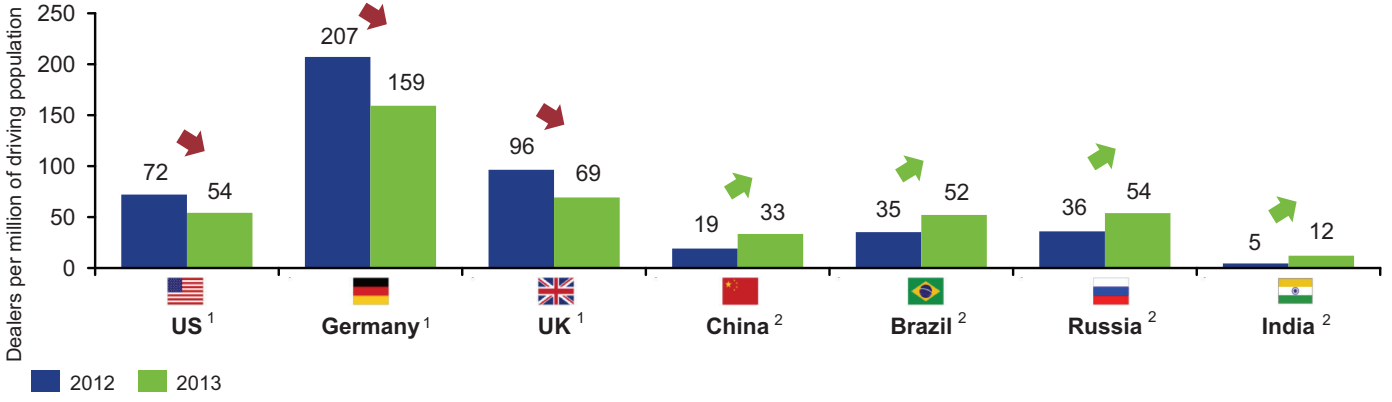
In contrast, population density is unlikely to limit the pace of growth in China, Brazil or Russia.

Of the top 10 sales markets in 2020, only Germany, Italy and Japan are projected to have a declining population density, which is not expected to impact these countries' high vehicle ownership rates.

The number of dealerships in the BRIC has to rise sharply to cater to the rising demand



The dealer network density in Germany is very high compared to other surveyed countries



Source: KPMG research & analysis, NADA, ZDK, SMMT, Urban Science, ANFAVEA, Avtostat, CarDekoh. [1] Assumption: Annual decrease of 3% until 2020. [2] Assumption: Stable sales per dealer ratio.

Key takeaways

Assuming constant sales per dealer, the number of new car dealerships in the establishing markets will have to increase sharply up to 2020.

China already has more new car dealerships than the US, and will have to nearly double this number over the next 7 years to satisfy steadily increasing demand. For the established markets, the trend is expected to be in the opposite direction, as competition will increase while dealership profits continue to decline.

Why is Germany's dealer network density so high compared to other mature markets?

The high dealer network density is a consequence of Germany's reunification. Eastern Germany's dealer network was heavily expanded in the 1990s, in order to cater to the sudden demand for new cars. Even by 2020 the number of dealers per million of population will still be considerably higher then anywhere else in the world.

Did you know?

Insights from the food retailing sector

Retail drivers and challenges

1 Aging population

The proportion of people aged 65 and above will significantly increase over the coming decades

2 Un-structuring of daily routines

Higher flexibility and spontaneity will make consumer behavior increasingly unpredictable

3 Technological progress, internet and social media

Internet-capable ultra-mobile devices will significantly change consumer buying behavior and increase the transparency and information level

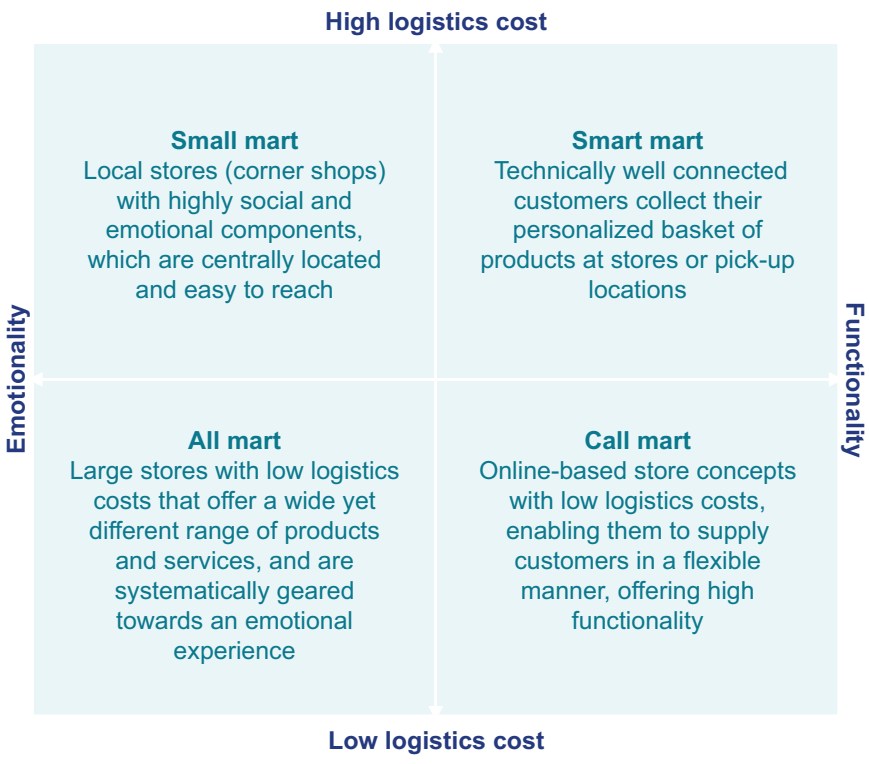
4 Rising energy prices

The steadily rising cost of individual mobility demands new types of transport and logistics solutions

5 Change of social and moral mindset

Consumers increasingly demand sustainable, healthy and environmentally-friendly solutions

Future food retailing scenarios



Don't you think that many of the drivers influencing the food retailing sector could be equally relevant to global automotive retail businesses in the future?

Source: The Future of Shopping; Outlook for the German and Swiss food retailing. A survey by GDI Gottlieb Duttweiler Institute and KPMG, 2013.

What could this mean for automotive retailing?

Derivation of future automotive retailing scenarios

Retail drivers and challenges

1 Aging population
The proportion of people aged 65 and above will significantly increase over the coming decades

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Higher flexibility and spontaneity will make consumer behavior increasingly unpredictable

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The steadily rising cost of individual mobility demands new types of transport and logistics solutions

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Consumers increasingly demand sustainable, healthy and environmentally-friendly solutions

@

Connectivity will be an enabler for all retailing concepts rather than a game changer for the auto retail sector itself.

Future automotive retailing concepts

High logistics cost

Emotionality

Flagship stores Exclusive stores in urban areas primarily focused on the emotional presentation of a selection of vehicles to strengthen the brand/ product reputation and awareness (often directly owned by OEMs)	**Traditional dealerships** Local PoS focusing solely on new car sales in the easy selling period. Range of offerings is further extended to used cars, service and after-market parts in a hard selling environment
Virtual stores with sales agents Web-based stores offering new and used cars. Physical customer contact (e.g. for test drives, home delivery) is organized online and executed by mobile sales agents	**Super stores** Very large outlets that focus on a high volume of transactions. Typically these outlets have large vehicle inventories, big showrooms and often have multi-brand offerings

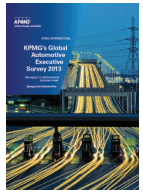
Functionality

Low logistics cost

Conclusion

The decision for the right retail concept has to be balanced between the customers' preference regarding emotionality/functionality and each market's maturity level.

KPMG's Global Automotive Thought leadership



Global Automotive Executive Survey 2013

**Self-driving cars:
The next revolution**

**Global Manufacturing Outlook:
Competitive Advantage**

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