After The Flood: What will happen to the dealership system?

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The OECD projects lasting economic scars to the UK economy – a 10% hit from Covid 19 and a further 5% from Brexit. The UK, already looking too much like a Latin American country, with a top layer of great wealth on top of a gig economy, is heading for severe impoverishment. This is already translating into the automotive sector.

The market for electric cars – still largely bought by those prepared to pay a large premium for ecological sanctity – has collapsed. The SMMT predicts a 30% year-on-year drop in the UK new car market to the end of this year. This is not caused by a lack of demand for cars. In an article of 2nd October, the Financial Times published an article entitled “UK lockdown drives used car prices to record growth”. It quoted Motor Trader to the effect that prices in September were on average 7.6% above those a year ago, having firmed up for all of the previous five months.

Car dealers, used to selling 2 to 3 used cars for every new one, were now selling 7 or 8. Scared off public transport, people needed more cars – these are additions to the fleet. Young people who had preferred apps to wheels were now flocking to take driving tests. This fresh demand, however, is at the “wrong” end of the market, coming from less solvent and sometimes desperate consumers. Retail customers had already largely deserted the new car market, even before Covid.

Franchised dealers can survive selling fewer new cars. In the volume brands they make precious little money on them. They make better margins on used ones, certainly at today’s prices. But they will get hit where it hurts, in the workshop, where they earn the majority of their profits: fewer cars in their first ownership cycle to work on at very high charge-out rates; and an accelerated defection of owners of used cars to cheaper independent repairers.
As they lose volume, they will be forced to increase workshop rates even more, and to be fewer in number, thereby making them even less price competitive and accessible, and thereby losing even more customers. A vicious circle.

In my last blog I identified the structural weaknesses and incoherence of the traditional automotive system of franchised dealerships. The combination of Covid 19 and a hard or very hard Brexit will administer a huge and, in my opinion, fatal shock to this system. But what will replace it? Cars will not vanish from our roads. They will still need to be sold, maintained, repaired, and re-sold. But by what means?

Franchised dealerships bundle together a number of functions that are in fact separate businesses. The ostensible reason is convenience for the car buyer and the reassurance of having the outlet that sold the vehicle take responsibility for maintaining and repair it. But consumers are now much more sophisticated and used to choosing different outlets and formats for different goods and services. They unbundle.

The real motivation for the bundling, as we identified in our work for the European Commission on the Automotive Block Exemption Regulation as long ago as 2002, is to secure near-monopoly rents in the aftermarket and thereby to cross-subsidize weakly profitable new car operations. This is achieved through abuse of both customers and dealers.

The different functions of the dealership do not need to take place in the same location. None of them are inherently specific to a given brand, except where customers wish it, as in up-market and specialist cars:

- **Product information**: already in the pre-Internet age, this function had largely been taken over by the numerous car magazines. One can now locate what one is looking for – new, near-new, used – at the click of a mouse.

- **Prospecting for customers**: it’s now customers that prospect for themselves, very largely. It’s simply about matching instantaneous micro-supply with micro-demand, and it can be done very cost-efficiently via the Internet. The platforms do not need to be brand-specific.
Selling: the traditional dealer price haggling process is detested by customers. Apart from eBay, consumers are now used to fixed prices in on-line commerce. Bang go the showroom and the salesperson.

Viewing and test driving: these can clearly be arranged via independent, all-makes centres, close to where the demand is – you don’t keep stocks of shiny cars there, you bring them in against appointments.

Pre-delivery prep: this can’t go virtual but it’s already performed by all-makes specialists in some cases.

Maintenance: routine service, has gone down in volume considerably over past years, as designs and component and build quality have improved so much. There’s simply not enough volume left to keep all those single-brand dealer workshops alive. Brand-specific product knowledge is to a large extent an artifice, intended to tie customers to the dealer workshop.

Diagnostics: this has become the manufacturers’ and dealers’ new-found line of defence against the independent repairers, thereby attracting the unfavourable attention of regulators, notably the European Commission. Not sustainable.

Repair: the same arguments apply to repair. If there is to be specialization, it is more logical to do it by type of intervention – as has long been the case in skilled body repair and de-skilled tyre fitting – rather than by car brand.

Spare parts distribution: this has long been a racket, with no real competition between the dealer and independent sectors (tacit alignment of list prices). The manufacturers make huge margins in this, the dealers much less. Some of this cosy establishment is starting to be shaken up, to the discomfort of many, with a massive threat from on-line purchasing replacing extensive local stocking. There is no justification for multiple distribution channels specific to car brands.

Short-term rental: this is long since mainly in the hands of independents, ranging from the international airport majors to local van hire. Facilitated by the Internet and possibly boosted in the longer term by reduced individual ownership.
• *Brand support:* this consists more of extravagant investment requirements placed on dealers by their franchisors than anything else. This is a luxury that will surely go.

We face a different world, in a Britain durably impoverished and altered in its motoring habits by the accident of Covid-19, and gratuitously self-injured through Brexit, unless and until the miracles promised by the Brexiteres come to pass.

The automotive industry in the UK will have been sold down the river by them – they have failed to extract any concessions for it from the EU. So they will have no further need to defend its costly Peculiar Institution, the franchised dealership system. Perhaps we shall end up like New Zealand, bulk importing used right-hand-drive cars from Japan.

There will be considerable opportunities to set up all-makes service and repair chains, which can also supply both new and used replacement cars. Keeping their existing cars in operation will matter more to most consumers than replacing them and impressing the Joneses. Managing chains of independent repairers has always been a challenge but newly-liberated dealer workshops could form a good core.

Dealer groups, newly focused on service to the customer, instead of being loose chains of tied manufacturers’ sales outlets, could lead the charge in this. But dealers will need to change from being the slaves of the manufacturers to the servants of the motoring public.