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Automakers say repair shops will kill car brands

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AUTOMOTIVE NEWS EUROPE

The new block exemption proposal has thrown the industry into chaos, say Europe's carmakers.

It's not just the rules announced last month by EU Competition Commissioner Mario Monti that have auto executives confused and angry. It's also the lack of detail.

"When dealers ask us what's going on we don't know what to tell them," said Earl Hesterberg, Ford of Europe's vice president for marketing, sales and service. "We don't get any answers."

ACEA, Europe's carmakers' association, has asked for a much more complete explanation of the proposal. But carmakers already see many problems, including:

- Separation of sales and service franchises that carmakers say threatens brands by turning repairs over to unreliable third parties.
- A reluctance by dealers to invest in their facilities because of uncertainty about the future.
- Disruption of efforts to restructure dealer networks.
- Emergence of big dealer groups that could dictate terms to carmakers.

The new block exemption could even change manufacturing and product development processes.

Current rules restrict the territories of authorized dealers and prevent them from selling multiple brands from one show-

room. Dealers must also provide aftersales service, and handle warranty work. All that is changed in the new EU proposal.

The Commission is scheduled to approve the new block exemption in early July. The current rules expire in October.

Carmakers say car prices across Europe will be harmonized — Monti's main goal. But they won't fall to the low wholesale levels now found in high-tax countries like Denmark. Some even say the harmonized prices will be higher.

But auto executives say Monti's biggest mistake was separating sales and service. Dealers will be free to find subcontractors to handle their service operations.

"I started out in service and I know that you can't sell a new car to a customer and then say, 'Goodbye, see you again when you buy another car,'" said DaimlerChrysler Chairman Jürgen Schrempp.

But that's where the industry is headed, said Schrempp.

"Dealers see a very dangerous situation," said William Helfer, an auto retailing specialist at consulting group Urban Science. "They see wild growth as all kinds of independent repair garages and chains expand. Because the manufacturer is required to give service literature, anyone who feels like they can repair a BMW and Mercedes can."

Helfer, who advises manufac-

turers on their dealer strategies in Germany, said carmakers have already begun to react. For example, Audi last month set up an audit organization to check independent repair shops. Others are expected to do the same. Still, carmakers say quality will be hard to control.

"This makes it much more difficult for recalls and warranties," said Michael Ganal, BMW's board member in charge of sales and marketing.

Carmakers could also lose access to service and quality data now fed back into their systems.

"If the information goes to a third party, it prevents the brands from talking to the customers," said Peter Stevenson, a specialist on block exemption issues at Urban Science.

Why would dealers give up their lucrative service operations?

"Dealers with service capacity constraints may subcontract," said Stevenson. "For example, Skoda with a relatively small car parc doesn't have enough service work. But Volkswagen dealers do not have enough repair capacity. So Volkswagen is vulnerable."

Uhland Burkart, Opel's management board member for sales and service, said he expects to "issue a number of service authorizations."

"The standards we have built



**Schrempp:
Service is
crucial**



**Hinfray:
Looking for
answers**

up are in danger," he said. "It is not clear if we are free to define standards. What quality criteria can we use? The details are a big problem."

Renault's top sales executive, Francois Hinfray, said the Commission has not made clear how the rules will work.

"We have to know what is the link between sales and service in the new regime," said Hinfray. "If Midas (repair shop) fulfils the Renault after-sales standards, is it mandatory to make Midas an after-sales partner of Renault? I don't know the answer."

Jacques Beherman, the Belgian distributor for Mazda and Saab, fears that dealers will go for cheaper parts.

"My dealers can source parts without giving me a chance to assure the quality," said Beherman. "What I can be sure of is that the dealer will charge the price of an original part. I'm not sure what kind of network will give the backup if we have to make a recall."

Splitting sales and aftersales is a huge problem, said Renault Chairman Louis Schweitzer.

"There are just so many loopholes," he said.

Nick Scheele, Ford's president, added: "To separate sales from service is silly."

Volkswagen Chairman-designate Bernd Pischetsrieder said passing service work to independents defeats EU emissions and safety objectives.

"We have to meet emissions standards but third-party service providers may not have the equipment and software to maintain our vehicles," he said. "But we are still responsible. This has to change."

Carmakers can choose either exclusive or selective distribution options under the proposal. By

choosing an exclusive system, they can limit dealers to defined geographical areas. But the exclusive dealer could sell cars through supermarkets and other retailers that have little or no technical backup.

The selective option allows them to set tough standards for premises, but dealers can establish outlets wherever they want. Carmakers say they won't choose the exclusive option.

"Exclusivity is an open game," said Ganal of BMW. "Because the dealer can involve re-sellers, probably no one will go for this process."

Ford's Hesterberg also said carmakers will probably choose to be selective, not exclusive.

"But it's pick your poison," he said. "Both are disastrous."

Geographical expansion allowed by the selective option could change the dealer landscape dramatically.

"We could have a very strong move into high density areas," said Opel Chairman Carl-Peter Forster. "That could mean that some local dealers will be under pressure."

Urban Science's Helfer said financially strong dealers "can just expand and behave like King Kong. These guys are winning and the lean guys are losing."

"If I always wanted to go to Hamburg and open a dealership and my manufacturer has always killed my initiative I can now do it," he said. "We see this happening. In Germany we have several very strong chains and

they are going to be very aggressive. They can advertise a weak guy to death and put him out of business. The new competition will be fierce."

Jonathan Browning, head of sales and marketing for General Motors Europe, says the rules "will likely to lead to significant consolidation of the [dealer] industry."

Hinfray of Renault adds: "Dealer groups will probably be bigger."

Carmakers are worried. "If 30 or 40 percent of our cars are sold by a big conglomerate they will tell us what to do," said BMW's Ganal. "But they don't care about brand shaping."

At the dealer level, Stevenson said consolidation will make existing dealers nervous and reluctant to invest in their facilities.

"Why should dealers invest if they think a big dealer is going to invest next door?" he asked.

Ford's Hesterberg agrees. "Most of our dealers are family-owned businesses," he said. "They want to know what their future is. They are not investing in their facilities. We won't have any cooperation from dealers if they don't know what is going to happen."

As a result, the new block exemption may disrupt the ongoing rationalization of bloated dealer networks. Most manufacturers are in some stage of terminating dealers. They want fewer, but stronger franchise-holders and streamlined organizations of main dealers, sub-dealers and service outlets.

But the use of termination clauses to renew networks will be affected by the proposal. Current distribution rules allow dealers two years' notice, but carmakers don't need to specify why they are firing a retailer.

Opel Chairman Forster said the rule changes are one reason Opel has begun downsizing its dealer network in Germany. (See story on Page 38).

"Two years from now we couldn't do it with the new rules," he said.

Carmakers could be encouraged to buy dealers to gain more control over their networks.

"We would prefer not to put our money into buying dealers," said Hesterberg. "But this does make you think about that."

Another way to control networks could be to restrict the availability of financing from the automakers' captive finance arms — both for new-car loans and dealer inventories.

"I would not start spreading the finance activities to other makes sold by our dealers," said BMW's Ganal.

Beherman offers floor planning to his dealers. But if one takes another franchise, he said "the dealer will have to get another line of credit."

"I will not floor plan the other brand," Beherman said.

Urban Science's Stevenson said that could be a dangerous strategy. He said: "The commission will come down like a ton of bricks on anyone who shows any kind of favoritism."

The new rules allow dealers to sell separate brands from the same showroom without dedicated management or sales staff. Beherman recently turned down a dealer who wanted to sell Skodas at his Mazda site because the brands compete.

"The dealer needed to fill up his work shop," said Beherman. "Adding a Skoda franchise would have been an impossible situation. But under the new proposal I would not have been able to prevent that. In the end he got a non-competing brand."

Renault's Schweitzer considers this a central issue — one on which he hopes the EU will compromise.

"If there is more than one brand, we need a separate showroom," said Schweitzer. "But more than that we need separate

sales personnel. The customer needs to know that he is talking to a Renault specialist."

The new proposal makes it easier for dealers to buy spare parts

directly from suppliers instead of carmakers. But Stevenson said the practice may not become widespread, except at the biggest dealer groups.

"Manufacturers give very good warranties on parts," he said. "If the parts fail, the carmakers cover it. The big dealer groups will source from suppliers, but for others it is unlikely to be efficient to deal with 30 different parts makers. There would be 30 different trucks coming in. The price may be lower but that will be canceled out by the other costs."

To get around the problem, Stevenson said suppliers might try to develop joint distribution methods such as common parts depots.

"What will happen is that the carmakers will get more competitive on parts," said Stevenson.

Renault's Schweitzer said two amendments to the first draft proposal that came out last month have already reduced carmakers' concerns in this area.



Hesterberg: Dealers won't invest

Warranty parts must now come direct from carmakers and spare parts made by suppliers must come off the same production lines as parts built for original assembly.

GM Europe's Browning said two management teams have been created at GM to study the implications of the new rules.

"One will study what it means in terms of dealer sales and service," said Browning. "The other will study what it means for our business model, including product development, manufacturing and a number of other upstream activities."

For example, he said the new rules could create a need for more flexible manufacturing to deal with the demands of

giant retailers that specialize in a limited line of high-volume, specially-priced cars.

"You need the right sort of flexibility if big dealers have a great degree of influence," said Browning.

BMW's Ganal said brand strength is still the key to managing networks.

"We will find ways to continue the exclusivity," he said. "If your brand is strong enough you can control your sales channel."



Browning



Pischetsrieder



Schweitzer