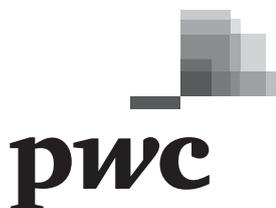


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Introduction



The global auto industry is always in flux, as new models and designs alter the shape and performance of automobiles. Nonetheless, few periods in automotive history match today's pace of change. Over the next five to 10 years, five trends will dominate, and each will carry with it specific challenges that auto industry executives will have to confront.

- *Self-driving will accelerate.* Companies will need to determine whether they can develop the technology to compete in this arena. If not, they may have to partner with a company that can better provide autonomous car technology. In addition, any companies hoping to be players in the self-driving market must consider the impact on supplier relationships and manufacturing operations, particularly what's needed to make these cars available in blossoming global markets in emerging nations.
- *Electric vehicles will take off.* This may offer an opportunity for automakers to meet increasingly strict CO₂ emissions requirements and to provide an array of new consumer and fleet products.
- *Connectivity will expand.* Connectivity, which is already having an impact, will expand to include a much wider range of features, such as car-to-X appliance communications. For instance, your home air conditioning system will automatically activate when you (and, more precisely, your car) are 20 minutes away. Automakers will have to build an ecosystem that includes partnerships with technology companies to develop connectivity features that stand out and attract consumers.
- *Profit pools will shift through new services.* Traditional carmaker business models are commoditizing, and OEMs need to reexamine their sweet spot in the value chain to address shifting customer needs. This could involve moving from car ownership to pay-per-use and ride-sharing services. But before choosing to enter this market, vehicle manufacturers will have to understand the full

costs of safety features, design innovations, and licensing rules in different global markets, as well as car-sharing overhead (parking, liability, and insurance) if they want to provide the services themselves.

- *Business models will become more local.* Operating globally has become significantly more challenging and complex. Automakers must find ways to understand and navigate the regulatory policies wherever they sell their products and wherever they have manufacturing facilities and suppliers.

These trends are just a snapshot of the imminent future for the auto industry. Not included in this snapshot are the many day-to-day challenges inherent to the modern auto industry, which we expect will only become more vexing as time goes on. Among them: required engineering improvements for the traditional internal combustion engine, anticipation of consumer design preferences, complexity management, pricing management, and the threats posed by new competitors moving into popular vehicle segments.

In this complex environment, auto companies can no longer hope to be everything to everyone. There are simply too many technical options, markets, and social and demographic changes to address. And as the competitive landscape intensifies, being average at many things will not be good enough anymore; companies will need to pick their bets and become great at the things that truly matter for the customers they have chosen to serve. Each auto company must be very clear about how it plans to add value for its particular set of customers; in other words, it has to confidently choose its *way to play*. And auto companies must determine which distinctive capabilities — that is, which unique processes, tools, knowledge, skills, and organization — will allow them to deliver on this value proposition better than anyone else and create a clear right to win.

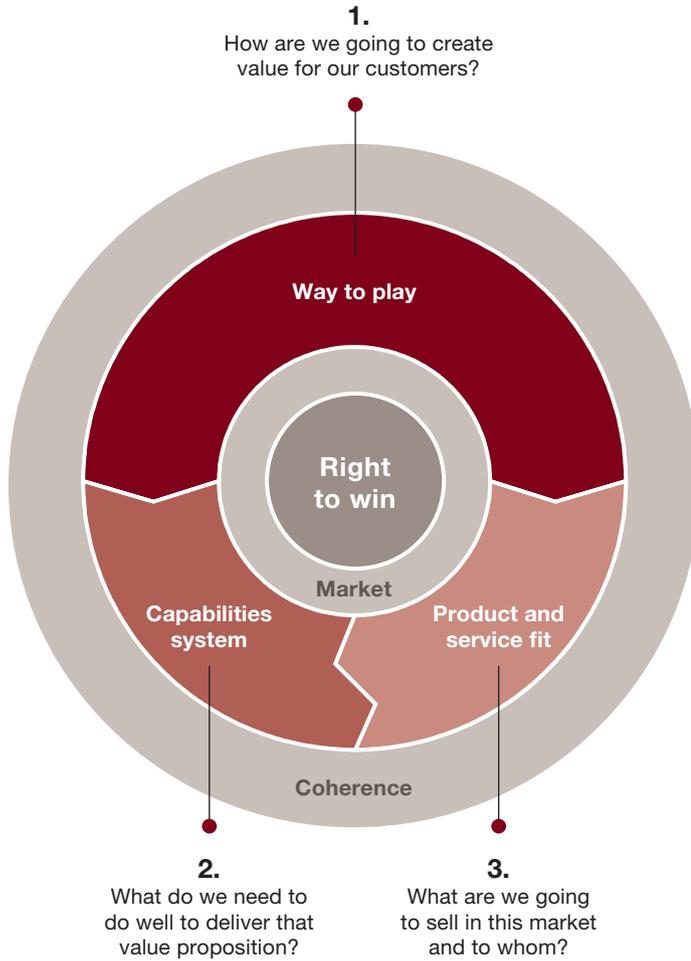
Armed with a coherent system in which distinctive capabilities, a strong way to play, and suitable products and services are aligned, automakers can generate sustained profitable growth. Such a coherent system is hard to copy, provides real value to customers, and differentiates companies from competitors (*see Exhibit 1, next page*).

According to our research, across all industries, coherent companies are three times as likely as firms that are incoherent to grow faster than the industry average, and they are 2.5 times as likely to generate higher profitability than the industry average. That is because coherent companies, by focusing on their few distinctive capabilities, continually improve in the parts of the business that matter most to their customers, and limit spending in areas that are non-

Coherent companies are 2.5 times as likely to generate higher profitability than the industry average.

Exhibit 1

The capabilities-driven strategy process is a powerful and effective way to think about this question coherently



Winning companies align their strategic direction to the capabilities that make them unique... they make hard choices about differentiation and stick to them

Source: Strategy& analysis

differentiating, such as unnecessary “lights on” or tables stakes capabilities (see Exhibit 2).

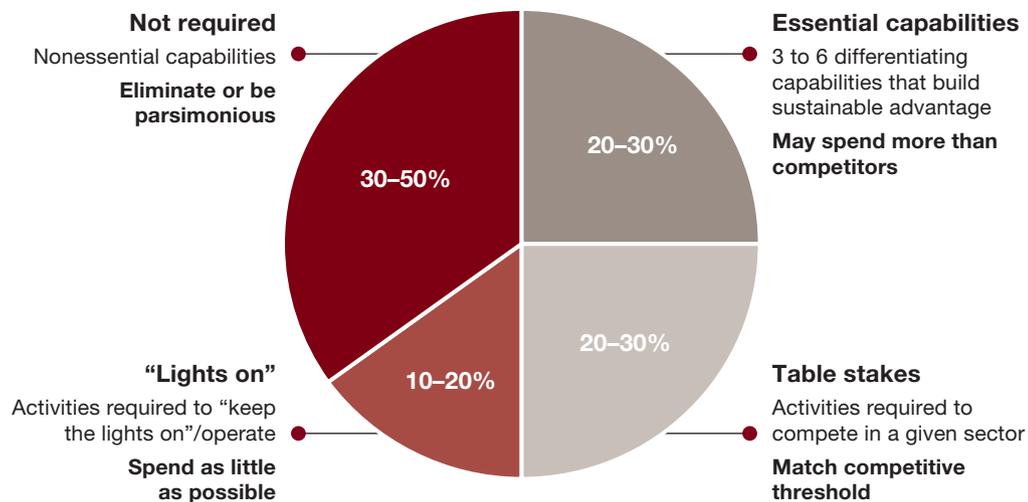
Moreover, companies demonstrating that they are passionate about their differentiating capabilities have more engaged employees and are able to recruit the best and brightest talent in the areas that matter most to them.

Selecting the coherent system that will give your company a distinctive advantage requires a thorough assessment of your company’s current strengths and the capabilities it can realistically develop, as well as penetrating insights into where the market is heading and what customers will increasingly demand. In our view, for automakers, there are currently nine archetypal ways to play, each of which has its own set of required capabilities. (More may develop in the future.) These archetypes can be categorized as either *traditional*, those that have been a part of the auto industry historically, and *emerging*, those that are fueled by recent technological or regulatory developments and changing customer behavior.

Exhibit 2

To determine required capabilities, place them in these four categories

Starting cost base breakdown



Source: Strategy& analysis

Traditional models

Experience providers. These companies build enjoyment, engagement, and emotional attachment through strong brands or experiences. Required capabilities include managing strong differentiated brands; managing a consistent brand experience across all models, geographies, and channels; and recruiting dedicated and enthusiastic employees.

Premium players. These companies offer high-end, high-prestige products or services from design through sales and after-sales services. Required capabilities include having the highest-quality research, development, and production activities and being able to take advantage of the latest breakthroughs in materials, technology, and performance.

Value players. These companies rely on efficient, scalable, and sustainable operations to provide low-priced vehicles and services often viewed by consumers as the best value for their money. Required capabilities include knowing how to prioritize cost optimization in R&D and procurement and leveraging scale and efficiencies in marketing, sales, and overhead.

Fast followers. These companies rely on the innovation of other auto companies to quickly introduce competing vehicles. In doing so, they often are able to provide greater value and sell to a broader base of consumers than the companies responsible for the design and manufacturing advances. Required capabilities include having efficient and fast-paced product development and production functions, leading fast followers to a shorter time-to-market than other automakers have. These companies also excel in market and competitor analysis.

Reputation players. These companies are viewed by consumers as trustworthy manufacturers and can charge a premium because of their good name in the marketplace. Required capabilities include displaying a strong commitment throughout the organization to maintaining and strengthening their reputation.

Emerging models

Regulations navigators. These companies find creative solutions for operating within regulatory boundaries and are able to offer customers in any region access to dependable, well-designed, and high-quality products. Required capabilities include making reliable predictions of regulatory trends and integrating those predictions into the R&D process.

Innovators. These companies consistently introduce new and creative products, such as electric or autonomous cars, or mobility and connectivity services. Required capabilities include accurately identifying new customer needs and market trends and finding ways to rapidly transform innovation into salable products and services. An open-minded corporate culture is often critical as well.

Solutions providers. These companies offer bundled products and services that address an unmet need in the market and adeptly focus on customer-oriented solutions instead of single products or services. Required capabilities include responding quickly to customer demands for innovation by bringing potential users into the development process and integrating disparate technologies and practices.

Platform providers. These companies operate and oversee shared resources. Required capabilities include having superior infrastructure with high availability and excellent user interfaces, defining and establishing standards, and building relationships with consumers on new channels.

It's important to note that choosing one of these ways to play and building the corresponding capabilities system does not guarantee sustained sector leadership. Automakers must constantly recharge their capabilities system to address changing trends and to further improve their value to customers, which in turn allows them to protect and enhance their competitive advantage. Depending on which model you choose to pursue, new trends will have a different impact on your capabilities system.

For example, when addressing the connectivity trend, a value player must focus on the best economic equation to maintain its niche as the

Automakers must constantly recharge their capabilities system to address changing trends and to further improve their value to customers.

provider of inexpensive, high-quality vehicles. In the calculus, the value player may share R&D costs and products with third-party companies, leverage off-the-shelf or non-custom technology, and be selective about advancing features. By contrast, an innovator should be agile and aim to lead in new connectivity developments; this type of company should control the potential breakthroughs in this area as well as influence the legal framework for implementing these features. Possibly, an innovator could also consider new markets to tap — such as mobility-as-a-service — that grow out of its connectivity designs (see *Exhibit 3*).

For automakers, the future is full of challenges but also tremendous opportunities. In this era, the industry is grappling with enormous and unprecedented shifts in powertrain design and vehicle technology. One thing is certain: In 10 years, the mix of new vehicles that hit the road will not at all resemble what we see today; on every thoroughfare there will be an amalgam of drivetrains, models, features, networks, vehicle-to-X communications, and artificial intelligence. To succeed in this landscape, automakers will need to ask themselves a fundamental question: “Who do we want to be?” In other words, “How should we be different to create value?” Automakers need to determine which skills, systems, processes, tools, and culture they can leverage or build to establish a differentiated way to play and implement a strategy that works.

Exhibit 3

How three different ways to play address the connectivity trend

Premium player	Value player	Innovators
Define the space you will dominate	Find a viable economic equation	Pick your play: accommodating or disrupting
Build global scale—beyond your brand	Share R&D burden through smart coops	Build on strengths: scale, agility, software
Test digital ventures; unlock data value	Test digital ventures; unlock data value	Occupy connected car control points
Move from transaction- to service-led setup	Shape and support mobility ecosystems	Reimagine greenfield mobility-as-a-service
Initiate a digital transformation	Innovate selectively	Get the legal framework to open up

Source: Strategy& analysis

How automakers can adopt a strategy that works

Achieving and maintaining a coherent strategy takes discipline and a willingness to chart an unorthodox path. In our research into some of the world's leading companies that apply such a capabilities-driven approach (PwC's Strategy& published the results of that research in *Strategy That Works: How Winning Companies Close the Strategy-to-Execution Gap* [Harvard Business Review Press, 2016], by Paul Leinwand and Cesare Mainardi with Art Kleiner), we have found that to build and maintain coherence, a company needs to undertake five unconventional acts of leadership:

1. **Commit to an identity.** Coherent companies don't get trapped on a growth treadmill, chasing multiple market opportunities, many of which they have no hope of gaining an advantage in. Instead, they are clear-minded about what they do best, developing a solid value proposition and building distinctive capabilities that will last for the long term.
2. **Translate the strategic into the everyday.** Many managers assume they should adopt the best practices of their industry and treat external benchmarking as the established path to success. But coherent companies view things differently. They translate the strategic into the everyday. They design and build their own bespoke capabilities that set them apart from other companies. Then they bring those capabilities to scale in their own distinctive ways.
3. **Put your culture to work.** A standard business practice for solving execution problems is structural change: reworking the organizational chart and rethinking incentives. The culture of the enterprise, if considered at all, is seen as a hindrance. But coherent companies resist disruptive reorganizations and instead put their current culture to work. They tap the power of the ingrained thinking and behavior that already exists below the surface in their company, using culture, not structure, to drive change.
4. **Cut costs to grow stronger.** A conventional company might try to reduce costs across the board by going lean everywhere. But the most successful companies cut costs to grow stronger. They marshal their resources strategically, doubling down on the few capabilities that matter most and pruning back everything else.
5. **Shape your future.** Coherent companies are not trying to simply become agile. They don't respond to external change as rapidly as possible. Instead, they shape their future by creating the change they want to see.

Do you have a winning strategy?

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