Eve of Disruption: How the Auto Industry Is Remaking Itself

written by Lauri Moon | October 12, 2016

Automakers are trying out all kinds of new business models, from rebranding themselves as mobility companies to partnering with obscure start-ups. Can they take it to the bank?

(IW – Laura Putre: 9-27-16) Although the U.S. automotive industry saw record sales in 2016, the mood of its leaders right now is low-key, even a bit anguished. Gains that OEMs made after the Great Recession have slowed to a near-halt, with predicted sales for 2016 hovering around last year's numbers, then dipping slightly in 2017.

Wall Street wants growth, and automotive manufacturers, realizing that they can't rest on their SUV and pickup-truck laurels, are looking for it in uncharacteristic places. Nissan is partnering with an electric scooter company in San Francisco. Volkswagen wants to focus more on car-sharing and introduce up to 30 new electric vehicle models. General Motors has a vice president of urban mobility who recently told an auditorium full of automotive executives that in New York City, where she lives, "the whole idea of owning a car, parking it for $1,000 a month, and not using it 95% of the time is ludicrous."

"Everything about our business is changing," Bill Ford, avuncular executive chairman of Ford Motor Co. and great-grandson of Henry, told a potpourri of Detroit automotive beat reporters, soccer-mom and fashion bloggers, radio hosts and foreign journalists at his company's trend conference in September. "It's been a tough time for the auto industry because Wall Street doesn't have a whole lot of faith in [us]."

Ford said some investment firms see auto companies as flatlining now that they've ridden a crest of post-recession growth. Or, they adopt the attitude that "with all this disruption, it's not clear to us who's going to win—what any [automotive companies] are going to look like in five years—so we're just going to take a step back."

More disruption is going on in automotive now than at any time since cars replaced horses as the dominant mode of long-distance transportation: After a long incubation period limited to annual DARPA challenges and whatever Google was doing in Mountain View, self-driving cars are on the fast track. Tech companies are muscling in on the traditional auto space. New mobility services like ride-hailing and microtransit are challenging the individual car ownership model.

Meanwhile, the price of cars is outpacing wages in the United States, and political uncertainty and economic stagnancy are slowing growth in some emerging markets. Electric and fuel-cell vehicles are gaining traction as their price tags come down and range goes up (along with fuel economy standards).

The auto industry has to think about all this and the Volkswagen emissions cheating scandal and finding tech-savvy people to run the factories and software engineers to design algorithms to tell a driverless car how to behave when a herd of cattle is crossing the road.

"It's not clear where some of these business opportunities really are," Bill Ford said. "We are going to try a lot of different things, and obviously we have to build business models around them that work, and I'm very confident that that will happen."

Until then: stay tuned for a considerable bit of rooting around in the dark.

Taking the Slow Road

Automakers looking for meaningful growth aren't likely to find it in the United States. Vehicle prices have been growing faster than wages, observes Patrick Manzi, senior economist for the National Automobile Dealers Association. Consumers are stretched: car payments made up 12% of personal income in 2014—higher than the previous nine years. And the loans take longer to pay off: 67 months in 2015, compared to an average 54 months two decades ago.

Paul Traub, senior business economist for the Federal Reserve of Chicago, says that automotive sales likely peaked in 2015. Some of the reasons he sees include a trend since 2010 of Americans saving more of their income; a depletion of pent-up demand for new vehicles after the Great Recession; shortened commutes for more people working remotely from home; and a shift in population from smaller cities and suburbs to "megacities" where mass transportation is convenient. People are also holding onto their new vehicles longer: from an average 50 months in 2005 to 77.8 months in 2015.

Even in the richest metro area in the country, San Jose, Calif., a median-income household cannot afford the average new vehicle, says Bankrate's 2016 Car Affordability Study.

Worldwide, car ownership climbs when average incomes hit the range of $5,000 to $20,000, says Gary Silberg, lead automotive industry partner for KPMG. Within that range, ownership leaps from one car per 10 people to one per two.

China is in that sweet spot for growth, but hurdles include car quotas in pollution-wracked major cities and regulations that require foreign automotive companies to partner with Chinese companies (and share their research).

India has huge potential, with about one car for every 30 people. But wages aren't high enough.

"If you talk to the auto guys, every 10 years they say India will be 10 years away," says Silberg. "It's a low-end, $10,000 vehicle market—kind of a nuts and bolts market," with the modest profit margins to match.

So where will the growth come from? If you subscribe to the iPhone theory that new features = people dashing to turn in their old products and buy new products quickly, then leaps in technology could benefit automakers. And if the self-driving, living-room-on-wheels models cost way too much for all but the wealthiest consumers, then replacing individual ownership with fleet-owned vehicles to share, hail and rent looks better and better.