A CAR WITHOUT THE COMMITTMENT

Automakers need to advance their business model

THE WORLD OF mobility is moving – and changing – swiftly, and over the past 18 months, car subscriptions have suddenly become an option to owning or leasing. Automobile subscription services let a driver choose a car from a portfolio of models so that they can use it as if it were their own. As with leasing, the customer pays a monthly fee that covers insurance, tax, repair, and maintenance. But subscription services provide the option of replacing the car every so often: Another battle for the customer interface.

THE BEST OF ALL WORLDS

The main advantage of the subscription model is that it reduces the cost of commitment while increasing flexibility. Sharing and rental do not lock in the driver for a long period – either to a particular car or through a large outlay of cash; the hassle and downside, however, is that a car may not always be available. Ownership, on the other hand, provides the convenience of a car always ready for use, but it comes with long-term commitments – either through a big onetime payment or by financing, which means carrying debt for several years. Leasing provides the customer with a car for a fixed period of time after which they can either purchase the vehicle for its residual value or return it to the leasing company; but, again, leasing arrangements lock consumers into lengthy stretches of continuous payments.

Car subscriptions are in harmony with the broader trend of consumers subscribing to a service rather than purchasing a product, similar to streaming movies rather than buying DVDs. Such plans often feature flat-rate agreements that offer flexibility and appeal to all age groups. A recent Oliver Wyman survey showed that 26 percent of Germans are interested in the idea of car subscriptions – though Americans are less keen, at just 14 percent. (See Exhibit 1.)

If automakers do not set up subscription offerings themselves, the services could become a potential threat. When startups buy up fleets of cars and lend them out to subscribers, they – not the car producers – are the main point of contact for customers. In a worst-case scenario, automakers could end up as mere suppliers to independent subscription services – a danger they face from the rise of other mobility services, too.

Manufacturers need to set up their own subscription services and learn from customer feedback how to turn them into viable businesses. Making such a business work will require building or deepening additional capabilities, such as customer-specific offerings that go beyond a particular car model, pricing oriented to customer value, and fleet management. Subscription services should focus on three main points: attractive plans, competitive prices, and effective operations.

THE LUXURY PLAN AND THE ECONOMY PLAN

Though the market is still in its infancy and the basic structure of subscription services is constant, our study shows a significant split in the market. Some people are willing to pay for a selection of top-grade cars; others are primarily interested in the subscription model's lack of hassle. More than half our survey respondents – 55 percent in Germany and 54 percent in the United States – preferred a relatively low-cost package: less than €500 a month in Germany and under $500 in the US. In Germany, 23 percent were prepared to pay more than €1,250 a month, while in the US, 26 percent would pay more than $2,000.

One clear advantage of the subscription model is that customers can – depending on the frequency allowed by their package – switch cars according to the season: for example, a cabriolet for the summer and an SUV for ski trips and bad weather in the winter. Around one-fifth of German respondents give their preferred frequency for model switching as either weekly, monthly, or quarterly.

That said, the most popular switching frequency is yearly, both in Germany (29 percent) and the US (34 percent). Moreover, the option for shifting more frequently is not seen as an important feature by respondents in either country: In Germany, 16 percent say it is the most important aspect of the subscription model, and in the US, 15 percent. More important to consumers is the availability of desired models, which was the number one concern for 35 percent of German respondents and 50 percent of those in the US.

COMPETITIVE PRICES

Many potential customers will get out their calculators and decide that, given their needs, a subscription will turn out to be considerably more expensive than traditional car ownership. Automakers, in our view, should use the leasing rate as their benchmark: If they can match that, then their offer might become an attractive alternative for, say, a household's second car.

Automakers' subscription services should also offer a variety of plans to cater to the needs of individual customers. Some consumers are simply interested in hassle-free mobility and will not want to pay more than they have to. Others are car enthusiasts who will want to try out different top-end cars, even if this costs much more. City dwellers, in particular, might be interested in intermodal offerings that combine a car and an electric bike.

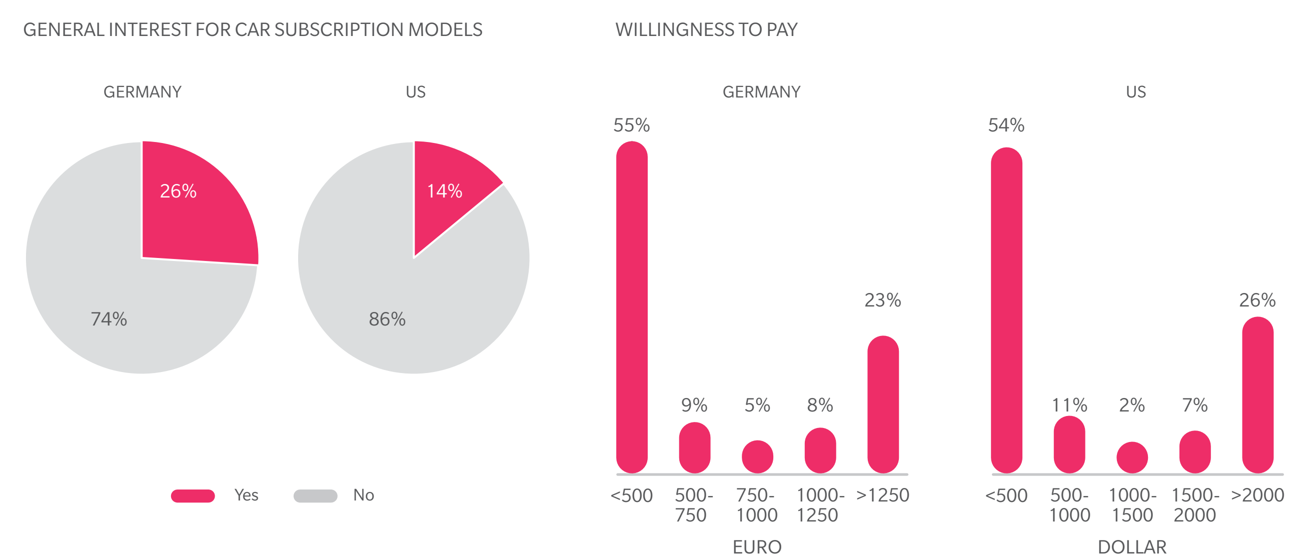
EFFECTIVE OPERATIONS

Fleet management is essential for holding prices down. Subscription services offer their customers relatively new cars – usually less than one year old. But a vehicle's first year is the period when its value sees the greatest depreciation, so the fleet should include younger used cars instead of new cars. Classic leasing price points will be the benchmark to compete with, and a holding period slightly longer than that for leasing generates additional subscription fees. Identifying the best time to sell the car requires strong skills in residual value management. Once vehicles get too old, they can be put into established remarketing channels, or other mobility offerings. Another solution will be to allocate the used cars to a car- sharing operation.

Fleet cars should be kept in use as much as possible and managed to minimize the depreciation in their residual value. Flexible pricing for peak and off-peak periods is one way to help vehicles surpass the breakeven utilization. One option would be to allow users additional switches (beyond the regular vehicle exchange schedule) at a lower price so that pooled cars are used more. Another would be to shift vehicles between different mobility services, for example by reallocating in-demand assets from rental to subscription. To maintain a car's value, the service operator needs to monitor its condition as it passes between different users, and to refurbish it when necessary. Overall, subscription services should aim for a system of integrated asset management,

EXHIBIT 1: GENERAL INTEREST FOR CAR SUBSCRIPTION MODELS

The offer of more flexibility for customers and how it gets accepted



Source: Oliver Wyman analysis

where each vehicle is used in different mobility modes, from subscription to rental to car share. An efficient operation will lower the costs of holding a car – and, therefore, lower the costs that have to be passed on to customers.

START LEARNING

Subscriptions may never be right for certain types of driver. One reason why the shift away from ownership has not been able to take hold among consumers is that people often have an emotional bond to their car, which is cemented by ownership. While many young people are no longer very interested in cars, that could change once they have families of their own and leave the city for the suburbs. So automakers should focus their subscription services on segments of consumers whose lifestyles are most likely to fit subscription services.

If subscription-service offerings are not done right, they could easily fail. Therefore, turning them into a successful business will be a learning process. As a first step, automobile manufacturers should set up their own subscription services and begin working out the kinks in them. If they do not, then someone else will instead – and it will be the other service that talks to the customers.

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