China’s automotive aftermarket: a strategic opportunity

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The explosive growth in China’s automotive aftermarket over the last decade has made China the largest automotive market in the world. While the focus has previously been on new auto sales, there has been much recent interest in the development of China’s automotive aftermarket. The domestic automotive aftermarket is in a relatively early stage of development and there are several characteristics unique to the Chinese market. Drawing from case learnings, the following article details some of the major issues and opportunities in the Chinese automotive aftermarket.

What is the size of the prize?

Driven by huge growth in new car sales, China’s stock of cars, especially older vehicles, is expanding dramatically. China has experienced annual growth of new car sales at 20 percent over the last 10 years, and strong growth is expected to continue. This is having the secondary effect of dramatically increasing the stock of cars in China. Furthermore, we estimate that by 2017 the average age of cars will increase from 3 years to 4.5 years, the age when spending on aftermarket parts and services will typically peak. This aging of the fleet is expected to result in the number of “out of warranty” vehicles dramatically increasing during the same period. This will further drive demand for aftermarket products and services, especially from the non-OES network.

Based on prior case experience we know that these factors are likely to create substantial demand growth for aftermarket parts and services. The size of the market has already increased dramatically from $10 billion in 2008 to $24 billion in 2012. This trend can only be expected to continue as China’s car fleet both increases and ages.

How are the aftermarket channels structured?

Understanding the value chain, key stakeholders and suppliers is crucial when developing a winning strategy. These will fundamentally differ based on the product type and manufacturer background, as well as by geographic market and development level of each city. As part of a growth strategy project for a leading U.S. automotive aftermarket supplier, L.E.K. defined the industry structure and identified attractive growth opportunities considering the market dynamics and the client’s core competencies.

A requirement was to build a dynamic picture of how the industry is expected to develop in the coming years. Currently, 4S stores hold the largest channel share in China, although chained repair shops are forecast to increase in relative importance in the coming years. Direct channels including self-owned/self-branded stores and online distribution currently account for less than 1 percent of the private car market, but may be positioned for strong growth. Besides the changes in channel mix another important trend will be increasing levels of industry consolidation. Government policy directives, including the 11th Five Year Plan, have been issued during the last decade aimed at decreasing the number of auto-component suppliers as a means of increasing scale and competitive capabilities. Additionally, a National Development and Reform Commission 2006 mandate encourages merger and acquisition activity in the sector. Every year we are seeing hundreds of domestic transactions in China’s automotive sector, which suggests the foundations of an emerging industry. A stronger home-grown automotive supplier base is gradually taking shape.

What are the customer segments and behaviors?

Customer demand is always critical in order to be able to determine the right strategy to succeed. L.E.K. was recently engaged to conduct a product development and consumer survey program to help our client form a clear understanding of automotive accessories needs and leisure trends of Chinese car owners.

Currently, most car owners use 4S stores for their after-sales needs. However consumers that purchase their vehicles privately (as opposed to company cars, government cars, etc.) are more likely to use non-4S service centers. These consumers are typically more price sensitive and may have greater automotive knowledge. However, the current presence of the OES network (i.e. 4S stores) is still dominant even in the private car repair market, and base business is 70% of the market.

Differences in consumer behaviors have been observed depending on what service or product is required. Consumers who require more crucial mechanical repairs, or issues concerning safety may be more inclined to use a 4S service center. However, for services including price, convenience, product availability or technical expertise influence or determine the service center selection.

Typically consumers have a preference for OEM parts, with the majority of consumers likely to choose 4S centers as their first choice. However, major surveys have indicated there are some regional differences in consumer preferences, for example, people in North-East China are more likely to prefer OEM parts.

There are also large differences between reported 4S auto part sales, and the estimated demand for 4S parts. This is likely due to a willingness to use other brands and the prevalence of counterfeit parts in the marketplace.

How do you develop a winning strategy?

The dynamic nature of the Chinese market means there are several key how-tos that will determine success. Consumers can be very price sensitive and there is generally low brand awareness. It is not uncommon for a BMW owner to shop around and save a few RMB on an oil change for instance – haggling for bargains is a key trait of the Chinese consumers and car-owners are no different in that respect. In such an environment it becomes critical to position the company correctly and align products, price and channel strategies accordingly.

In China, the component supply chain is long and complicated, and there are typically many levels of distributors. Design and management of the go-to-market and supply chain sales will determine success or failure in the industry.

For further information about the article or to discuss how L.E.K. can assist, please contact lekchina@lek.com