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Premium Brand Strategy in the Automotive Industry What are the characteristics of a successful Premium automotive strategy?

A Master's Thesis submitted for the degree of
"Master of Business Administration"

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Vienna, 31/07/2014

Affidavit

I, **Dr. László András Horváth**, hereby declare

1. that I am the sole author of the present Master's Thesis, "**Premium Brand Strategy in the Automotive Industry- What are the characteristics of a successful Premium automotive strategy?**", 78 pages, bound, and that I have not used any source or tool other than those referenced or any other illicit aid or tool, and

2. that I have not prior to this date submitted this Master's Thesis as an examination paper in any form in Austria or abroad.

Vienna, 31 July 2014

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Signature

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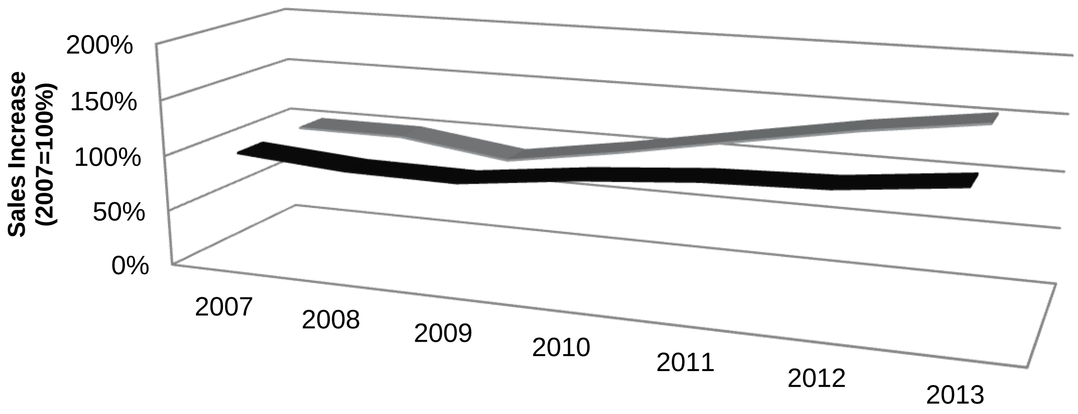
Chapter 1: The definition of a premium automotive brand

1.1 The problem-setting and purpose of the thesis

Premium is a very fashionable word in today's society – we want to live premium, even if it's meaning is not clear, or at least everyone has a thought on the personal meaning. It is associated with something affordable for the middle classes but allowing a glance of luxury: drinking a Nespresso in the morning, and if our Tag Heuer watch shows us we are almost late, just getting into our BMW, hit 200 km/h on the (German) motorway and arrive to work. Of course this was only an example, and the situations and brands could be freely interchanged.

But do the sale of this "premium life" to the customer pay well? Are customers willing to pay a higher price for such automotive products? Statistics answer with a clear yes. The pioneers of this segment, the German premium brands Mercedes-Benz, BMW and Audi showed that investing in premium products is worth the money and working time, if manufacturing the right products and sell it in a right way to the right people.

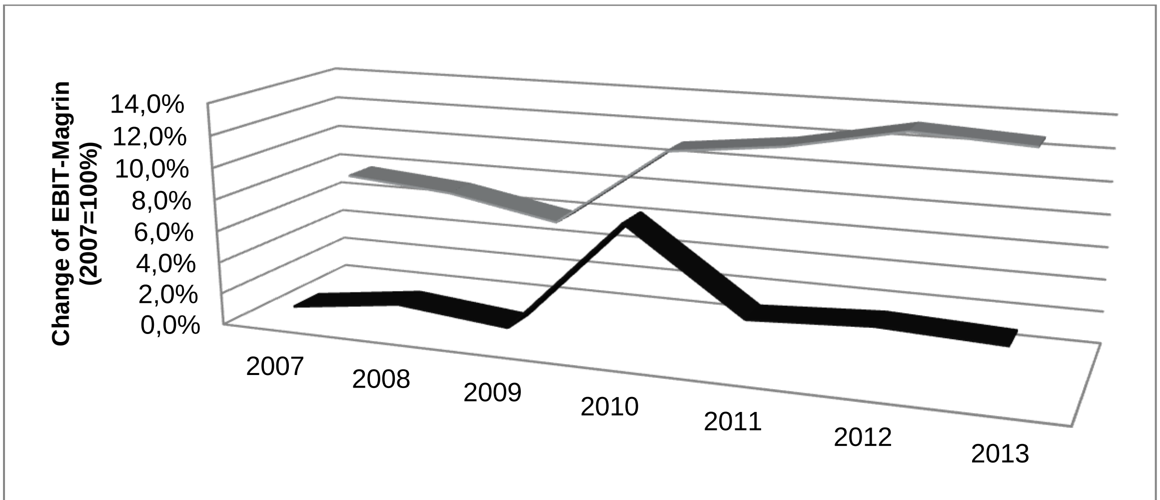
First of all the *customers' side*: Premium products have become more popular in the past two decades, as never before. The segment of these products is a good way for the successful players to steadily increase sales: Premium car brands in the past years were more effective in terms of growth (see *figure 1-1*). The crisis of 2008-2009 also effected the premium brands, but after the revival their sales boomed in comparison to the volume brands.



	2007	2008	2009	2010	2011	2012	2013
■ Volume Brands Avg.	100%	93%	92%	104%	112%	115%	127%
■ Premium Brands Avg.	100%	100%	86%	102%	121%	139%	153%

Figure 1-1: Yearly growth of sold cars (cumulated value of Volkswagen Cars, Renault and Ford vs. Audi, BMW and Porsche), author's research

More importantly, respectively for the shareholders most importantly, premium car producers were way more *profitable* in the past years, as shown in *figure 1-2*:



	2007	2008	2009	2010	2011	2012	2013
Volume Brands Avg.	0,9%	1,8%	1,1%	8,2%	3,2%	3,6%	3,3%
Premium Brands Avg.	7,8%	7,2%	5,9%	11,0%	11,8%	13,2%	12,8%

Figure 1-2: Change of EBIT-Margin (cumulated value of Volkswagen Cars, Renault and Ford vs. Audi, BMW and Porsche[1]), author's research

With the success of the German premium car brands and the customers' ability and willingness to pay the price premium for such cars shifted the automotive business towards a "new game" as K-H. Kalbfell formulated[2] – whereby the upper, more profitable price segment is expanding, as shown in *figure 1-3*:

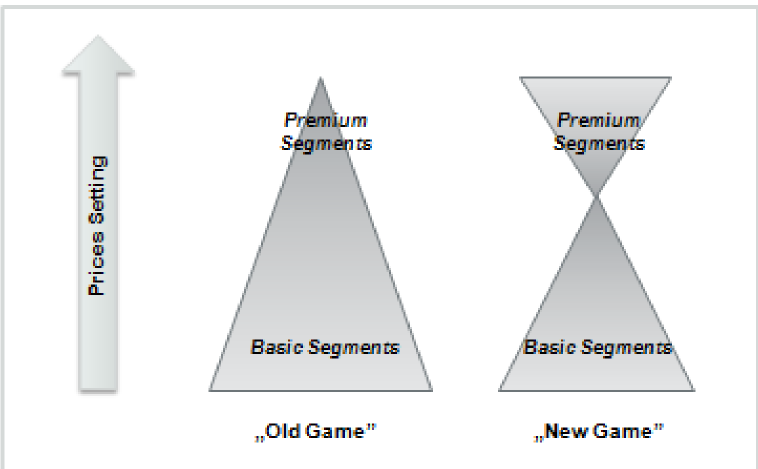


Figure 1-3: The "old game" and the "new game" ("Polarisierung der Nachfrage (Prinzipdarstellung)", K-H.Kalbfell, in. Gottschalk, p.265)

These factors drew the attention of other major automotive players as well – Nowadays top automotive groups have at least one premium brand: Toyota (Lexus),

[1] At Figure 1-2, the respective values of Porsche were not considered for the years 2007-2008-2009 because of the distorting effect of the financial activities in these years. At the volume brands 2007 and 2008 low values are due to Ford's losses of these years.
[2] Source of chart: in. Gottschalk, p.165

Renault-Nissan (Infitniti), Fiat-Chrysler (Maserati and Alfa Romeo is planned to be turned to a premium brand), GM (Cadillac) or Ford (Lincoln).
But what makes all the difference between premium and non-premium producers? If premium means extra profits, should not all OEM-s struggle to upgrade their brands and products into premium? What are the barriers, what are the risks?

The purpose of this thesis is to look behind the "right products" and the "right way" to build up and/or lead a successful premium brand, in particular to identify the key areas of an OEM-s strategy, where a different approach is needed, if compared to a volume brand or a budget brand and also to identify differences between diverse premium strategies based on three case studies.

1.2 Structure of the Master's Thesis

The Thesis is divided into four chapters.

Chapter 1 and 2 serve as a theoretical introduction. Chapter 1 is to give an overview of the topic – examining the definitions of the "premium" brands, including the identification of the boundaries to other brand segments. Chapter 1 also gives an overview about the benefits of the premium strategy and a rough overview of the key players of this market segment. In Chapter 2 I will examine the particular strategy fields, where the different approach compared to a volume brand is of the highest importance. In the present thesis, the strategy fields are limited to some key issues: innovation (research and development), sales-brand building-marketing, finance, production, HR and general organization.

Chapter 3 is the empirical part of the Thesis. After the identification of the key strategy fields, in the case studies of Chapter 3 I will examine the theory in the real world; three undoubtedly premium brands with three completely different best practices – A traditional luxury brand, one of the first ones in the world, "downgrading" itself to a very successful premium brand (Mercedes-Benz), the opposite: one of Volkswagen's daughters' very deliberate way to upgrade itself from mass to premium (Audi), and BMW's approach to revitalize Britain's iconic (but before the takeover far from premium) brand MINI and to lay down the foundation for premium cars in the small car segment.

Finally, Chapter 4 is to summarize the results of the best practices and to give a rough outlook into the future of the premium car market.

1.3 Added value that is paid: Definition of a "premium" brand

The word "praemium" originates from Latin and can be translated to reward or price. In German, the word "premium" stands for "*of exceptional, best quality*"[3]. The Oxford Dictionary[4] defines the word "premium" as "*an amount to be paid for a contract of insurance*" related to the insurance business, a meaning similar to the original Latin

[3] http://duden.de/; the German origins will have a significance, described later on in this chapter.
[4] http://www.oxforddictionaries.com/

as "*something given as a reward, prize, or incentive*" and a third meaning, as "*a sum added to an ordinary price or charge*". Beside the German association with quality, this third meaning is the fundament for the definition of premium in the sense we are looking for it in the automotive industry: premium means a high quality in some terms, and a price premium that the customer is willing to pay compared to a similar product.

The word "premium" is an often used phrase in the marketing world, as well as in everyday life. Beginning with premium cars of course (Products of the German "triad" of Mercedes-Benz, BMW and Audi, but also Lexus of Toyota, Infiniti of Nissan, as well as Jaguar or Land Rover can be considered members of the premium segment), but the phrase is also applied in the FMCG industry (Fast Moving Consumer Goods – e.g. Clinique), in the fashion industry (e.g. Louis Vutton, Emporio Armani) or even in the catering trade (e.g. Starbucks Coffee).

Premium is usually associated with high quality, some special features and – as mentioned before – a higher price. But what is premium or what is a premium brand indeed in the automotive industry?

Premium in the automotive industry is said to have its roots in Germany[5]. Until the time of the post-war period, there was a clear differentiation of mass and luxury in the automotive industry. There were on the one side the traditional luxury brands, like Mercedes-Benz, Rollsy-Royce or Cadillac (typically chauffered-cars, cabriolets, extravagant sports cars), while on the other side there were the brands which aimed to mobilize the people (Volkswagen with the Beetle or Fiat with the Topolino or the 500). This classical split was questioned during the oil crisis, the 70's and the innovation the mass producers of Europe and Japan managed in these times. The technology of the classical luxury brands became obsolete (huge and thirsty engines, expensive manufactural production) and they had to make their choices – for e.g. Rolls-Royce and Bentley stayed in the super-elite segment, and lived of their heritage, while Mercedes-Benz invested vast amounts into innovation (new and leading concepts with regard to e.g. safety, or consumption) and positioned itself lower than the super-elite brands, but absolutely over the volume brands. Mercedes-Benz was followed in the 60's from below and with a sporty image by BMW, and in the 80's by Audi also moving from volume to premium with an emphasized technical innovative image.[6]

Premium as such (an industry, a brand or a product) does even nowadays not have a unitary definition. The following definitions are only some examples trying to explain these terms, but help understanding the core concept:
"*A premium brand is a brand, which succeeds with its products to achieve a higher price in the market than other brands with similar products, which offer tangible functions*."[7]
"*A Premium brand is a brand that holds a unique value to a market through the design, engineering and quality that is provided*."[8]

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[5] And in some opinions not only in the automotive industry: According to some brand specialist, the first company to use „premium" as a predicate or quality feature was the company König-Pilsner Brauerei, again a German company, a brewery, with the „Warsteiner Premium Bier". in: Bracklow, 2004, p. 42
[6] Rosengarten and Stürmer, 2011, p. 21-23
[7] Kapfer 1999, p. 320

“*Democratization of luxury*.”[9]
“*Upper ranged branded products*.”[10]
„*Brand of the mass need, which is to be found in the upper price and quality segment, is in line with the buyers of the brand in the experience trade*.“[11]
Silverstein and Fiske define the typical premium products of BMW, Mercedes-Benz or Starbucks Coffee and alike as “*new-luxury goods*”.[12]
Rosengarten and Stürmer see premium car brands to have the following distinctive features: *“differentiation from luxury and mass brands, strong positions on their domestic market, and the high value of their used cars”* (low depreciation).[13]

Taken into account the varying definitions in the literature we can summarize the definition in a way that a premium automotive brand is characterized by the following factors:

1. the brand itself has a high symbolic value (According to Diez, the sources of a premium brand can be derived of three major values: Prime value (value of applied technology and used materials), Labor value (production process and country of origin) and Symbolic value (the psychographical value of the brand or semiothical relevance of the product).[14] The brand is investing a lot in maintaining and further expanding its high symbolic value (DNA of the brand, or brand heritage, or for example sponsoring events that are close to the “the brand’s identity”).
2. The products of the brand have trend-setter technologies, and the brand is investing proportionally more into innovations compared to volume brands.
3. Both the products and the brand itself have a high quality image. The quality imaged is rather an associated quality and applying leading technologies, but the premium brands are not necessarily the leading brands in the reliability surveys. Reliability can be very well differentiated from the quality image and customers’ own feeling about quality. On the example of Mercedes-Benz: in its darkest times in terms of quality, in the early 2000’s, Mercedes models were at the very back of reliability statistics, nevertheless they were considered as „reliable” by Mercedes-Benz drivers as well as drivers of competitors.[15]
4. Premium is not luxury. Premium products are usually produced in greater lots, and are not characterized by e.g. craftsmanship, which is typical for a luxury product.
5. Last but not least a vital factor is the consumers’ willingness to pay the price premium for these products (compared to products of similar level of mass producers), as well on the new car as well on the used car market.

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[8] http://www.saabhistory.com/2008/06/03/so-what-is-a-premium-brand/
[9] Kennedy 2012, p. 2
[10] Kapferer, 2009, p.43
[11] Markenlexikon.com: Markenwissen A bis Z, Kilian
[12] Silverstein, 2003, p.1
[13] Rosengarten and Stürmer, 2011, p. 26
[14] “Strategiewahl – Premium oder Massenmarkt”, in Gottschalk, 2009, p. 127
[15] For example in a survey of 2002, the C-Class was rated on reliability as Nr. 49 from different modells, while S-Class as Nr. 112 and V-Class as Nr. 150 (Nr. 1 was the Toyota Carina). At the same time 88% percent of Mercedes-Benz drivers and 61% of drivers of other brands considered Mercedes-Benz as a relaible brand (source: AMS 2002, Mercedes-Benz, Car Check 2000, Mercer Management Consulting).

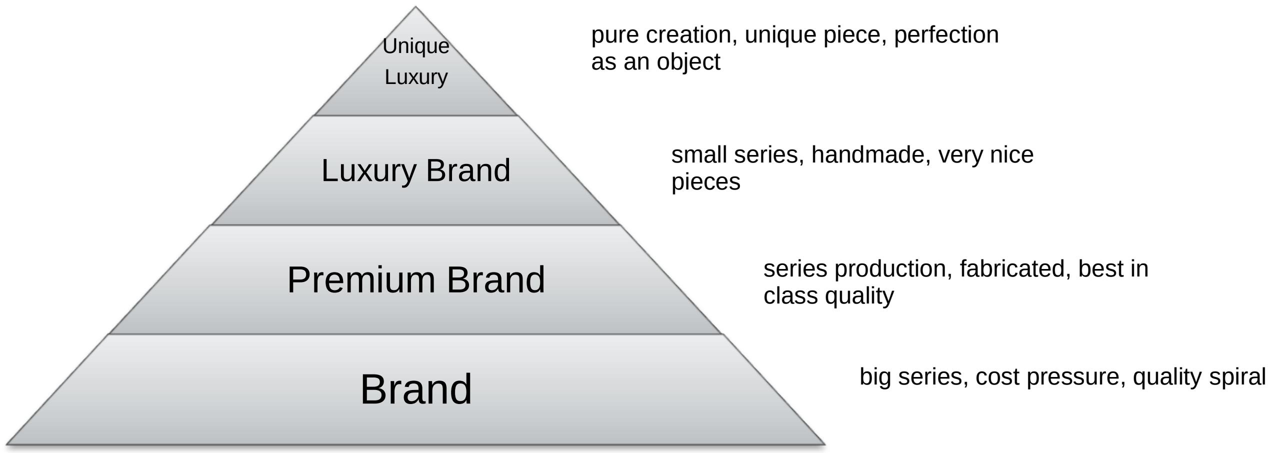
1.4 Differentiation between other categories, and subsegments within premium

After defining the “premium brand” it is essential to examine, what are the characteristics of brands which are not premium and how can they be characterized?

Different ways of defining brand classes:
If we can define premium as such the question automatically arises: what are the other classes if not premium? Some of the commonly applied differentiations are the following:

Mass – Premium - Luxury
Products and brands are typically differentiated into three segments: mass, premium luxury. However, it is really difficult to define the frontier between the categories, furthermore there also other ways to define, what is “not a premium” brand or product.
Mass brands are the brands with huge volumes, big economies-of-scale effects and cost-effective technologies.
A luxury product is produced in significantly lower scales, and the luxury appears on the “psychogrpahical” level[16]. This means a luxury appearance, usage of high class materials (leather, wood), and features which are also associated with high class society (e.g. LED-stars in the interior of the recently ceased Maybach brand, or a refrigerator for champagne in a Rolls-Royce). Also according to some opinions, purely from an economic perspective, luxury does not need to be differentiated from premium, since the “level of luxury” is characterized only by the price premium.[17] Rosengarten and Stürmer go even further: in their theory luxury brands are not characterized of innovation at all, the price premium is paid for size and comfort (so called “*American Luxury*”, e.g. GM’s ceased brand Hummer) or for the heritage and finesse (so called “*European Luxury*”, e.g. Aston Martin).[18]

The system of luxury and the brand[19]
Kapferer positions a premium brand also between luxury and a (mass) brand in the following way:



[16] in: Gottschalk, 2009, p. 129
[17] Kapferer, 2000, p. 323
[18] Rosengarten and Stürmer, 2011, p. 26, p. 164
[19] Kapferer, 2001, p. 352

Figure 1-4: System of Luxury and the Brand (Kapferer 2001, p. 352)

Middle Market – New Luxury – Old Luxury[20]

Silverstein and Finke's U.S. based theory differentiate between classic middle market products, the traditional luxury products and the newly emerging segment of New Luxury. Middle market brands and products are typically consumed by the middle-class and had their biggest boom in the 1950's when after Worlds War II there was mass demand for previously non-existing products, products existing in relative small scales, or luxury products (car, TV, refrigerators, etc.) on the one hand and an industry capable to produce it on the other hand. Luxury brands are typical brands of the high classes. New Luxury are the "premium" products, more expensive and more sophisticated than middle market, but not of the traditional old luxury brands – the New Luxury can be further divided into three subcategories as "accessible superpremium", "old luxury brand extension" and "mass prestige (or masstige). Examples from the automotive industry: middle market brand: Pontiac, Ford; new luxury: BMW, Mercedes-Benz, old luxury: Cadillac, Rolls-Royce.

1.5 Another way to reach the profitability of premium brands: value brands

Further to the distinctions described above, the terms "value brand" or "budget brand" (brands positioned between mass and premium), using the unclear frontier between the two categories, like was introduced as a concept by Renault with the Dacia brand and is a great success since the introduction of the Dacia Logan in 2004. Low cost products are designed with the main emphasis on the lowest possible end consumer price, by using existing technology and low-wage production sites (by Dacia, it is the existing Renault technology and e.g. the Romanian base plant of Pitesti) – by keeping the costs down, using the effects of economies of scale, Dacia is now the key element of Renault's global strategy ("*really a cash cow for the company*")[21]. Even in 2014 there are not many low cost brands like Dacia (notwithstanding the dozens of domestic manufacturers of cheap cars in China, who are making up their "budget brand" since they have no approach to sophisticated technology), the competitors cannot be clearly defined: maybe Skoda or Chevrolet in Europe could be considered as a value brand. In the meanwhlie Renault goes even further and is introducing the Dacia models also under the local brand Lada in Russia[22].

1.6 Key players of the premium car market

[20] Silverstein, 2003, p.3

[21] As told by Reanult Chief Operating Manager, Mr. Carlos Tavares in an interview. Dacia has an operating margin of about 9 percent which is the niveau of not even mass, but rather the premium brands. in:Automotive New Europe, Global Monthly, December 2012. Dacia's 42% increase of European sales in Q1 2014 is giving 19% of the Renault Group's total sales increase. in: http://www.inautonews.com/renault-sales-strong-but-q1-revenue-still-slips

[22] Some automotive players keep their brands (as a prestige increaser), but develop budget models, like Dacia. Such is for e.g. the Peugeot 301 or Citroen C-Elysee

Several premium brands could be identified in the actual global car market, nevertheless the following incomplete list gives a rough overview of the brands who play a major role:

BMW

The BMW Group is one of the most successful premium car manufacturers, with two premium brands, the core-brand BMW and MINI (see chapter 3.3), as well as the traditional exclusive luxury brand Rolls-Royce. BMW was established in 1917, firstly dealing with airplane engines, the first car model was the Dixi (originally an improved version of the Austin Seven) in 1929.

BMW Group's sales went to all-time high in 2013, with 1.964 million units (1.655 million units BMW, 0.305 million units MINI, as well as 3,630 Rolls-Royce cars), with a group turnover of € 76.06 billion and EBIT[23] of € 7.99 billion.[24]

BMW is traditionally strong and the leading brand in Europe and north America (here competing with Mercedes-Benz and Lexus), while it is in big battle with Audi in the Asia-Pacific region.

Mercedes-Benz

One of the very traditional luxury-premium brands established in 1885. For detailed history, see chapter 3.1.

Historically Nr. 1 among the premium brands, but after years as Nr. 3 (in terms of volume) after the competitors BMW and Audi, in 2013-2013 Mercedes-Benz is again on the very hard way to the top of the premium brands with 1,467 million sold units in 2013. In the business year 2013 the division Mercedes-Benz Cars (including the Mercedes-Benz and Smart brands) reached a revenue of € 64.31 billion, and EBIT of € 4 billion[25].

Audi

A technique oriented premium brand, part of the Volkswagen Group. For detailed history, see chapter 3.2.

Audi delivered in the business year of 2013 for the first time more than 1.5 million vehicles to its customers (1.575 million cars sold in 2013) the goal of the strategy "Route 15", reached two years earlier. The revenue of Audi in 2013 was € 49.88 billion and EBITDA[26] of € 7.1 billion[27].

Porsche

A traditional supersport-car manufacturer established in 1931 by Ferdinand Porsche originally as technical consulting company (Ferdinand "Ferry" Porsche was the chief constructor of the famous Volkswagen Beetle before World War II), but the first Porsche car, the 356 was built in 1947. Nevertheless, the brand – even before the takeover by Volkswagen – switched strategy at the beginning of the 2000's from supersport-car manufacturer to a classical premium manufacturer (but keeping its sporty image) with the launch of the full-size premium SUV Cayenne. Porsche is since then heavily expanding its sporty, but not sports car portfolio in the upper class of the premium segment (e.g. 4-door coupé Panamera, mid-size SUV Macan).

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[23] Earnings Before Interest and Taxes
[24] BMW Group Annual Report 2013 (http://annual-report2013.bmwgroup.com/reports/bmwgroup/annual/2013)
[25] Daimler AG Annual Report 2013
[26] Earnings before interests, taxes and depreciation/amortization
[27] AUDI AG Annual Report 2013

Porsche - now as part of the VW group - also reached its best year in terms of sales in 2013 with 162,000 units (15% increase compared to 2012). Porsche is among the most profitable car manufacturers, in 2013 with a turnover of € 14.33 billion and EBIT of € 2.78 billion.[28]

Lexus

Toyota's Lexus subsidiary introduced its first model, the LS 400, tailor made for the U.S. market in 1989, and laying down the foundations of a new premium brand (The brand Lexus was not even introduced in Japan until 2005). Lexus is a great success since then with the highest rate of loyal customers, however the success is not expanding to the European market, where Lexus has little market share compared to its German rivals.

Lexus's planned sales of 520,000 units in 2013 half of which sold in the USA.[29]

Infiniti

The other major Japanese brand also wanted to take its share from the premium market and founded Infiniti in 1989 (Infiniti was introduced even later at the Japanese market only in 2013, so for these "Japanese" brands actually the U.S. is the domestic market).

The brand is still relatively small, with sales of 173.000 units in 2013. Infiniti is still in brand building with strong foundations on the U.S. market and costly sponsorships, like of the world champion Formula 1 team of Red Bull.[30]

Cadillac

Cadillac is a traditional luxury/premium brand of the U.S car manufacturer giant General Motors. Established among the very first car brands in 1902, Cadillac has a long tradition in luxury – it lived the golden ages in the 1950's and 1960' with iconic premium full-size cruisers, like the Eldorado or DeVille. Despite multiple efforts, Cadillac still could not take a solid foot on European soil, and its market position has also heavily shrink in the past decades, with the traditional competitor on its domestic U.S. market Lincoln (belonging to the Ford Motor Company), the Japanese and German rivals.

Cadillac reached worldwide sales of 250,000 units in 2013 a year-on-year increase of 22% to 2012.[31]

Tesla

Tesla is a newcomer, a boutique start up in the premium automotive business, focusing on BEV[32] premium cars, founded in Palo Alto, California only in 2003 with the first model, the Roadster in 2008. The breakthrough was the introduction of the Model S in 2012. Tesla managed to sell more than twenty-thousand Model S in 2013 and however it is still not profitable[33] it is on the best way to become a major premium player on the BEV market where it is already dominant.

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[28] Dr.-ing. h.c.F. Porsche AG Annual Report 2013 (http://www.porsche.com/international/_malta_/aboutporsche/overview/dataandfacts/)

[29] http://www.reuters.com/article/2013/11/20/autoshow-tokyo-lexus-idUSL4N0J50VR20131120

[30] Nissan Annual Report 2013

[31] GM Global Sales 2013 (*http://media.gm.com/dld/content/dam/Media/gmcom/investor/2014/jan/2013-GM-Global-Sales.pdf*)

[32] Battery Eletric Vehicle

[33] EBIT in 2013 was $38.47 million – source: *www.wikinvest.com*

1.7 The benefits of a premium brand vs. benefits of a mass brand, brand-portfolios

It is a vital decision of a car manufacturer to define its brand and its products on the mass to premium scale (at the case of luxury brands a decision about placing the products on the aforementioned scale is rare, but if given the tendency is usually a downward brand extension like in the example of Maserati or Porsche), in order to build a strong brand with profitable products. Not only a premium brand can be strong, and not only a premium brand can make big profits.

Benefits of a premium brand

The most important factor for the company is of course the price premium. Premium products enable through the price premium higher average prices and over proportional profit ratio. As shown in figure 1-2 premium players have higher profit ratios, and the past years show that the sales volume (generating the high incomes) is also over-proportionally growing if compared to volume brands.
A good premium brand is a very strong image builder, but on the other side a well maintained image and tradition is also a precondition for a premium brand. The brand must invest in keeping and building it heritage, this is possible also from the higher profit ratio.
Very simplified: premium brands reach higher profits, which must be again reinvested into innovation and brand building which again enables premium profits as show in Figure 1-5.

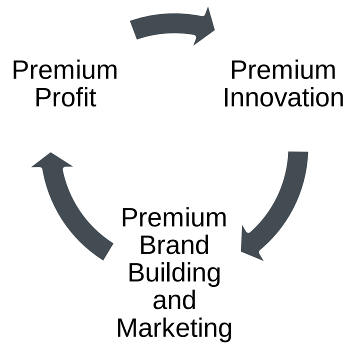

Figure 1-5: The premium profit circle (author's chart)

Benefits of a mass brand:

Mass brands (and as mentioned before, even low-cost brands) can produced great profits. Nevertheless, the profit ratio is typically and significantly lower, than in the premium segment, but this is very well offset by the economies-of-scale effect of producing in much bigger scales.
Development costs play a vital role at premium brands. In their case the development costs are usually higher than at mass brands (the need for fancy and state-of-the-art technologies), and of course the economies-of-scale effect is also in this case a relevant benefit for a mass brand.
Price is a much bigger concern when buying the product, than image or technology. The image does not need to be polished by costly motorsport participation or expensive marketing promotions. Nevertheless; an effective marketing is at least of same importance, as at premium products.

Brand Portfolios
The key players of the automotive industry are well aware of the aforementioned benefits (and also disadvantages) of the single brands, which made most of them struggle to build a brand portfolio. This can lead to a complete coverage of the vertical market from mass to premium (or even to luxury)[34] and enabling to use all the synergies this system offers, namely to reduce production and development costs of premium cars and at the same type the mass brands can access to state-of-the-art technology. A common dealer-platform is a great advantage for both sides: the dealer can offer a bigger variety of products, on the other hand the manufacturer can place its premium products on more dealerships (but not in every case - an odd example: a lot of Volkswagen dealers in Germany also sell and repair Audi, which would normally enable the VW Group to have a better reach to customers than the competitors Mercedes-Benz of BMW, however according to recent statistics in Germany it was true for the service partners against both competitors, but BMW had more sales partners in 2013 than Audi did)[35].

The following table shows some typical passenger car brand portfolios of the different major automotive groups as of year's end 2013, based on the differentiation mass-premium-luxury:

	Mass/Value Brand	Premium Brand	Luxury Brand
BMW	-	BMW, MINI	Rolls-Royce
Daimler	-	Smart, Mercedes-Benz	-
FIAT	FIAT, Alfa Romeo, Lancia, Chrysler, Dodge, Jeep	Maserati	Ferrari
FORD	Ford, Troller	Lincoln	-
General Motors	Chevrolet, Opel/Vauxhall, Buick, Holden, Alpheon	Corvette, Cadillac	-
Renault-Nissan	Renault, Nissan, Dacia, Samsung	Infiniti	-
Toyota	Daihatsu, Toyota, Subaru	Lexus	-
Volkswagen	Skoda, Volkswagen, Seat	Audi, Porsche	Bugatti, Bentley, Lamborghini

Figure 1-6: Brand portfolio of some of the key automotive players as of end of 2013 (source: author's research)

1.8 Summary

In this chapter the most important features of a premium automotive brand were defined: that is to have its brand heritage with a high symbolic value; it must be trend-setter if it comes to innovation; it should possess of a quality image; its products are

34 in: Gottschalk, 2009, p. 141
35 Sales Partners/Service partners in Germany, 2013: Audi: 471/1051, BMW: 569/133, Mercedes: 401/464 (source: *www.de.statista.com*)

manufactured in greater lots with best available technology; and the customers will buy the products of this brand for a premium price, which must be reinvested to keep the above mentioned premium features. The synergies can be used with mass brands, like splitting developments costs, which is one of the main reasons, why the leading automotives groups are managing brand portfolios consisting of volume and premium brands as well.

In the next chapters I will examine what kind of strategy on the different fields of business must be applied and how this in real life works.

Chapter 2: Brand strategy: What makes a premium brand differ in its core business from mass producers?

2.1 Significance of the strategy choice

Should a CEO of a premium brand make the same decisions during operation and planning of the future of its brand, as her/his colleague who is leading a mass brand?

The method

A premium automotive product is much more than only a nice label and a higher price. Manufacturing a premium automotive product and operating a premium automotive brand differs in many aspects – as described in chapter 1 – from the processes of a typical mass producer. According to Diez these two worlds are based on completely different business models.[36] This should mean, that the whole business is different, thus strategy decisions on different spheres of business require a different view and decisions, then on the "conventional" mass-business.

In the following chapters, I will examine some of the most typical business fields (R&D, marketing, finance, production, HR and general organization) of an automotive OEM in order to determine the key points, where a different strategy is required from a premium manufacturer.

What kind of strategies are there?

The premium strategy can be best observed from the perspective of Porter's three generic strategies[37]. Porters generic strategic rule describes the businesses' strategy choice to achieve and maintain competitive advantages. Porter identifies the three best strategies. They are: cost leadership, differentiation, and focus (focus is one the strategies according to Porter, but it is viable from both aspects: cost, as well as differentiation). Market segmentation is narrow in scope while both cost leadership and differentiation are relatively broad in the scope of the market. Porter's competitions strategies are shown on the following figure:

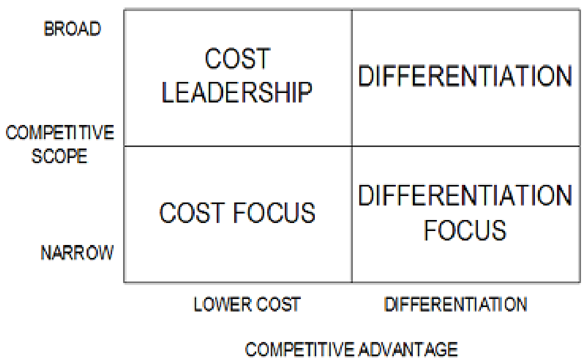

Figure 2-1: Porter's theory on the competition strategies

A company is for all successful, if it concentrates on one of the three strategic approaches. To put efficiency as top priority and thus be able to sell for the best (lowest) price, to differentiate the products from other (creating something unique), or

[36] in: Gottschalk, p. 142
[37] Porter, p. 35

to focus your efforts on a niche, only a part of the markets (usually suitable for smaller enterprises). A company must keep to one of these strategic approaches and try to avoid to "stuck in the middle" between the different strategies, which can with great probability cause failure.

Applying these strategies to the automotive industry, we can identify the three different strategic approaches in the following chart:

Figure 2-2: Porter's competitive advantage theory applied on automotive industry
(based on chart in: Rosengarten and Stürmer, p. 222)

Cost leadership is typical for mass producers, where the company must stay as lean as it can get in order to achieve profits (e.g. Toyota). Differentiation is the basic strategic element of premium car brands, while Ferrari can be considered to have a niche strategy (high differentiation with a narrow market scope).[38]

Of course premium brands cut costs, where it is reasonable, but the main emphasis is on differentiation, and creating something of more value to the customer, that is worth the premium price as described in Chapter 1. How this strategic approach appears in the typical business fields are examined in the following sub-chapters. Due to the limits of the present thesis, the examined business fields are the ones, where a premium business must be of greater distinction to volume players – divided into six sub-chapters these are: innovation, brand building, sales, financial results, production, and general organization including HR.

2.2 The method to examine the premium strategy in the particular business fields

The assumption of this Master's Thesis is that premium brands have different approaches in all the six defined business fields and these can be identified in specific values or other facts. In order to be able to compare the different values and facts we also need competitors – it is not necessary to compare all the players, so I decided to choose three premium and three typical volume brands: Volkswagen, Renault and Ford, as well as Audi, BMW and Porsche. Volkswagen is a huge volume brand possessing a differentiated brand portfolio[39] (part of which is Audi and since the recent year also Porsche – where only group data could be assessed, Audi/Porsche is also part of the results, however the differences can be well observed if comparing VW Group results to pure Audi/Porsche results). Renault is

[38] Rosengarten and Stürmer see Porsche's strategy as a niche strategy, however the first publication of their book "Premium Power" was in 2003, when Porsche could really be considered as a niche brand, but nowadays with sales volumes corresponding to of Cadillac and having several models (SUV's, limousine, sportscars) place the brand in my opinion rather to "Premium Power".
[39] see figure 4.

also one of the great global players (and has the Nissan subsidy Inifniti as a smaller premium brand, but its effects are not comparable to Dacia for e.g. – most data exclude Nissan and its brands). Ford is another major global player with U.S. roots (its premium brand is Lincoln – since it is not a separate company data always include Lincoln, but Lincoln's market share is globally marginal and is thereby not relevant). BMW is a typical premium brand and the BMW Group also consist of only premium or luxury brands (Data is usually from the BMW Group, so this data includes Mini and Rolls-Royce as well).

Differentiation categories	Volume Brands			Premium Brands		
	Volkswagen	Renault	Ford	Audi	BMW	Porsche
Innovation						
Brand building						
Sales						
Finance						
Production						
General organization						

Figure 2-3: Sample chart for the presentation of the strategy differences

2.3 Innovation

Trend-setter technology was defined as one of the core elements of a premium product. Innovation in every aspect (inner and outer design, powertrain, infotainment, etc.) is a must for a premium brand.

Several technologies in the automotive industry were first introduced in the premium classes for two main reasons: nomen est omen - as described before, a premium brand must be innovative and secondly, the customers of a premium product are more touched by innovations, ready and able to pay a price premium for new technologies. Examples for technologies debuting first in premium cars are for instance ABS (developed in cooperation with BOSCH, first in series in the S-Class of Mercedes-Benz in 1978), airbag (although many OEM-s experimented with it, first car in series production with driver's airbag was again the S-Class)[40], all-wheel drive in a passenger car or aluminum space frame (ASF) body-technology (both Audi, from 1980, and 1993), or a sophisticated multimedia-interface commanded by a single button (i-drive of BMW from 2001, introduced first in the 7 series) and carbon fiber body-technology in greater series (i-series of BMW in 2013). Also typical: the costly innovations come first in the top models (e.g. segments D and E) of the premium brands, because here is the biggest requirement for state-of-the-art technology, and the customers ability and capacity for paying these innovations are the highest in these segments as well.

Hence innovation and thus product development is identified as top priority, premium brands need a different approach to their R&D strategy:

1.) Importance of R&D:
Premium means leading in technologies and not copying or being second. Even if in a group, R&D is a central issue, only some of the competences are centralized (for example Audi has its own R&D department consisting of several thousand engineers,

[40] Baun, p. 8

it is cooperating with VW's R&D division and even some developments topics are split between them, so Audi has a lead function at some important development topics within the whole VW Group). Typical for a brand portfolio of a group is, that the newest technologies appear in the models of the premium brand first.

2.) Investing in innovation:
The importance of this point was detailed above and in Chapter 1: R&D expenses of premium brands are proportionally higher than such expenses of mass brands.[41]

3.) Eagerly searching for new segments:
As explained with Porter's theory, the premium brands are focusing their strategy on differentiation. A very typical example is offering the right custom-made car for the customer. This means not only the tailor-made production instead of lean production (see Sub-Chapter 2.6 for details), but also a pursuit to offer more and more derivates suiting to the customer's (with good marketing activities generated) needs. Thus, a vital focus of R&D is to develop new car segments and derivates[42].

4.) Cooperation within the automotive industry:
Premium brands are not necessarily part of a big brand portfolio, it can happen that they stand alone (or can be leading brands of a group themselves, like BMW and Mercedes-Benz, however the BMW Group and Daimler AG are of smaller economic power than VW, Toyota or GM).
If the premium brand is not part of a big "family" and thus have less resources, cooperation with mass brands is typical in order to save on R&D costs. A current example is the struggle of the premium brands to sell volumes lower than their traditional market: the global partnership of Daimler and Renault-Nissan (The comprehensive partnership was announced in 2010 and also confirmed by interchange of some stocks. Inter alia the partnership's results were the Mercedes-badged urban delivery vehicle based on the Renault Kangoo, cooperation for delivering engines and a common platform for the new Smart fortwo and Renault Twinigo, introduced in the Geneva car show in 2014[43]) or BMW and Toyota (Based on the cooperation announced in 2013, BMW and Toyota contracted for the joint development of a fuel cell system, joint development of architecture and components for a sports vehicle, and joint research and development of lightweight technologies[44]).
Cooperation is not limited to other OEM-s. Cooperation between key automotive tier-1 supplier companies and OEM-s are also typical (e.g. with Bosch) – this is not unique for the premium brands, but it can happen a premium brand can afford to develop a highly complicated part itself or in cooperation with the tier-1 supplier, while

[41] An example of 2005: R&D expenses of BMW were amounting € 1.8 bn., while in case of Hyundai € 120 million, thus BMW invested for each manufactured car 15 times the amount Hyundai did! (*Rund 70 Prozent der F&E-Wertschöpfung werden durch Zulieferer und Entwicklungsdienstleister erbracht; http://www.car-innovation.de/fileadmin/user_upload/pdf/downloads/charts_pm_car_innovation_2015.pdf*

[42] In 1985 Audi had 5 models (the Quattro, 80, 90, 100 and 200 series), while today there are dozens more, but similar examples could be stated for BMW, Mercedes-Benz and in the recent years, also for Porsche.

[43] *http://www.caranddriver.com/news/daimler-and-renault-nissan-announce-global-partnership-car-news*

[44] *https://www.press.bmwgroup.com/global/pressDetail.html?title=bmw-group-and-toyota-motor-corporation-deepen-collaboration-by-signing-binding-agreements&outputChannelId=6&id=T0136503EN&left_menu_item=node__804*

mass brands tend to buy the component completely developed by the tier-1 supplier, who has a greater R&D knowledge of the component[45]. Yet, suppliers play a more and more important role also in the business of the premium brands.

3.) Inter-industrial cooperation:
In the last decades, especially in the electronic industry, the speed of development is immense. Electronic, Computer- and – increasingly – mobile phone technology are becoming a great part of the automotive business and the main field of future R&D activities. Already invested themselves a lot into these technologies, nevertheless premium automotive players still lack the in-depth know at example battery-technologies for BEV-s or sophisticated infotainment systems. Of course premium brands are not the only ones to participate in such cooperations, but since they are the ones needing mostly the up-to-date technologies, they are among the first to do so. Examples for such cooperations are Audi and Google[46] or Daimler and Deutsche Telekom (the partnership formed in 2013 is sharply focused on providing new online services and web applications for use in automobiles - such services include real-time traffic information, mobility options, personal radio and access to social networks[47]).

4.) Key R&D fields must stay in-house
Also not an exclusive prerequisite of premium brands, but more typical is, that the key R&D fields are not outsourced to Tier-1 suppliers or purchased from competitors. The key DNA of the premium brand is in its powertrain, its interior and exterior design.

How to measure these factors and what can we insert in a table in the sense of Chapter 2.2 that is a measurable and objective KPI? I considered the following criteria as important measurement indicators in terms of innovation:

- ***Expenditure on R&D***: First of all, premium brands are supposed to spend a lot more for R&D, than volume brands – a good indicator for this hypothesis is the KPI which shows how much did the sample companies spent on R&D in proportion to their total sales revenue? The sample year is the last available business year (2013), the source is the annual report of the said companies[48].
- ***Number of derivates***: According to the assumption in section 3.) above, premium brands invest vast amounts for the development of models, in order to conquer newer and newer segment. Indicator for this factor is, how many different derivates the sample companies have. Considered here are the number of different passenger models (without LCV-s and Trucks) all models on sale according to the respective home pages on the domestic market of the sample brands as of 30/04/2014.
- ***Recent and total number of patent applications***: For R&D the number of patents is also a good measuring number. In this respect to different KPIs are considered: the number of patent applications in 2013, and the total number of patent applications on the sample company name (Volkswagen AG, Renault

[45] Typical examples are complex modules like gearboxes, like the Company ZF (delivering gearboxes for BMW, Porsche, etc.) Source: http://www.konstruktionspraxis.vogel.de/themen/antriebstechnik/getriebe/articles/308116
[46] in: Wall street Journal: cooperation between Audi and Google to introduce android in the infotainment system; source: *http://online.wsj.com/news/articles/SB10001424052702304591604579288670734733740*
[47] *http://www.telekom.com/media/enterprise-solutions/179862*
[48] For exact sources, see literature

S.A.S., Ford Motor Company, AUDI AG), Bayerische Motorenwerke AG and Dr. Ing. h.c. F. Porsche Aktiengesellschaft). Source for the numbers is the internet website “patentdocs”[49]. In the applications, the company names are sometimes used multiple times for different applications – basis of the comprehension was the official company name with most of the patents, an exception was VW, where the number of patents for both Volkswagen AG and Volkswagen Aktiengesellschaft showed a significant number, so in this case the patent numbers were added.

Differentiation categories		Volume Brands				Premium Brands			
		Volkswagen	Renault	Ford	Volume Avg.	Audi	BMW	Porsche	Premium Avg.
Innovation	Expenditure on R&D / total revenue (in %, as of 31/12/2013)	5,80%	4,43%	4,59%	***4,94%***	7,95%	6,30%	11,17%	***8,47%***
	Number of derivates	24	27	17	***22,67***	48	39	7	***31,33***
	Number of patent applications in 2013	40	48	22	**37**	132	67	24	***74***
	Total Number of patent applications as of 30/04/2014	110	401	129	**213**	325	427	249	***334***

Figure 2-4: Innovation

The table confirms the above assumptions in these measurable terms. The sample premium brands spend 1.7 times as much on R&D. Premium brands have also 50% more models, than volume brands (even taken into account that Porsche does not have a complete portfolio and is correcting the result downwards). Patent applications also show the clear leading position of premium brands (a correction on the volume side is here Renault, with more patent applications than both Porsche and Audi).

2.4 Brand building and Sales

Rosengarten and Stürmer define the marketing concept of premium brands as “*marketing worth for your money*” – a tight business idea, on the basis which the customer groups are identified, the strategic product portfolio constructed, the necessary competences and finally present and market the company as well as the products suitable to the targeted customer groups[50].

The significance of brand building has already been emphasized in chapter 1.6. A strong brand is a vital component in the premium class. Strong brands usually have deep roots and heritage (however there exceptions also from this term: Lexus was introduced in 1989 as a brand new brand – still, with its design perfectly suiting to the US market and its excellent quality made it a great success) and they are basis for the customers’ identity with the brand and also their brand loyalty. Nevertheless the

[49] *www.faqs.org/patents/*
[50] in: Rosengarten and Stürmer, p. 214

strong brand image is also a factor for which the customers are ready to pay the price premium.

Regarding sales and marketing volume brands can be just as innovative or even more innovative, than premium brands. Nevertheless premium brands (even because of the other distinctive factors like innovation and strong brands) have it easier to reach high sales but the methods and targets are usually different.

The key factors and differences in terms of brand building and sales in the premium class are the following:

1.) Transfer of innovation-primacy to the brand
Innovations and brand building go hand in hand. Innovation is needed for brand building, since one of the key strategies is to bring the innovations near the customers[51] and strengthen the brand.
A very typical element, the witches kitchen, where innovations are made and what transfer greatly innovative image is motorsport – to be successful in motorsport is one of the oldest recipe to establish car brands, several car brands proved it[52]. Classic premium brands have great motorsport traditions: all the three big German brands make up today's DTM[53] field, Mercedes is involved in the Formula 1 on the highest class, as was BMW, while Audi is engaged in the endurance racing, being one of the most successful brands with 12 wins in Le Mans and the Audi Quattro (or S1) was/were rally legend(s) in the 1980's. Porsche also has long history both in Le Mans, on the race tracks, but even in the Dakar series. Infiniti is building up its motorsport image, e.g. in 2012-2013 as sponsor of Red Bull's Formula one team.

2.) Brand history and the Premium heritage
There are plenty of volume brands which have their roots in the beginning of the 20th or even at the end of the 19th century (e.g. Ford or Renault). History is an important feature of a premium brand but it is even more important how this history is kept, groomed and communicated, furthermore the key core, the DNA of the brand must also be defined and consequently used / developed[54].
Brands also have a message, however cars of the high premium cars are much more alike, than ever, still the brands have different "missions" best described in the slogan of the brand. Good examples are Audi ("Vorsprung durch Technik" officially translated to "Truth in Engineering" = Audi stays for innovative technique-oriented products) or BMW ("Freude am Fahren" or "Sheer Driving Pleasure" = driving BMW cars is fun, quality of driving is more important than other features).

3.) Sponsoring
Part of the brand building is also spending money on events or teams which reflect the premium image of the brand. Such examples are the sponsoring of elite football teams (like FC Bayern Munich or Barcelona by Audi) or typical sports of the targeted

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[51] in: Rosengarten and Stürmer, 2011, p. 179
[52] M. Winterkorn: Audi . Innovation, Technik und Design, in. Gottschalk
[53] DTM stays originally for „Deutsche Tourenwagen-meisterschaft", German Touring Car Championship, which is absolutely international today
[54] Ken Roberts identifies the following rules for managing a brand's "true value": 1. Understand and respect the brand, 2. Understand the true target audience of the brand, and 3. Understand what can and should not be changed in the brand. in Gottschalk, p. 105

customers, the upper middle class (e.g. sailing, ski-events by Audi or golf and tennis events by Mercedes-Benz) or motorsport as mentioned at Point 1.).

4.) Image transfer from and to other brands and products
Premium brands often use cooperation with premium brands from other fields of industries. Typical is the cooperation with renowned producers of sound systems (e.g. Bose and Audi or Burmaster and Mercedes-Benz). Several premium brands broaden their product portfolio and strengthen their image by offering clothing and lifestyle products (Porsche Design is a very good example for this).

5.) Pricing and trims
Regarding pricing, the main goal of a premium brand is to be able to exert a price premium. But how big is this premium the customer needs to pay?
At a concrete example, a Ford Focus 5dr with a 1.6 l TDCI engine of 95hp costs 15.980€, while a similar size BMW 114d, 5dr, also 95hp costs 24.900€[55]. This corresponds already to a difference of 36%. Further price premium can be reached through the trims and options. The base trim of a premium car is usually not at all more luxurious than of a volume car. But there is a possibility to order the same and a lot more options (including the more innovative features as describes in chapter 2.3.) which makes it possible that the price difference between volume and premium is at the end of the day with mix improvement a way more than at the base trim versions.
But premium brands go even further. They offer to satisfy any need of the customers if its paid for. The tailor-made trims (like Audi Exclusive Line or BMW Individual) can generate further extra over proportional profit for the premium brands.

6.) High residual value
High residual value is a very important factor for premium brands, since the higher residual value, or higher price of a used car makes the customer's decision to purchase a new car instead of a used one easier (less price difference between used and new). High residual value leads also to better leasing rates, which is very favorable for fleet customers.
High residual value originates on the one hand from the fact that cars of premium brands are indeed really looked for also on the used market. On the other hand premium brands also have their methods to encourage high residual value: Such a policy is, that for example premium brands usually do not give producer's incentives (like incentive credits or price reductions) like most volume brands to boost sales, thus the incentives for new cars do not have a value reducing effect on the residual value of the used cars. Another example is Porsche, who introduced in 2003 on the U.S. market an incentive program of giving 2-3,000$ surplus on the value of the customer's used Porsche, if he or she decided to buy a new one (this way parallel boosting sales and help maintaining high residual value).[56]

7.) Customers and markets
The main difference is of course between volume and premium, that the customers of premium brands are willing to pay the price premium as described above. These customers are usually configuring the car of their own (this is why premium brands

[55] Base trim in both cases. source: *www.ford.de*, and *www.bmw.de*, data as of 30/04/2014.
[56] in. Rosengarten and Stürmer, 2011, p. 31

usually build to order – BTO - instead of raising bigger stocks - BTS)[57]. Also, fleet customers are choosing (at least in Western Europe) in higher proportion premium brands, because of the above stated effects on high residual value and leasing rates. Rosengarten sees also the strong domestic market as a major contribution for the premium manufacturers through the effects of the cars delivered for the management and employee car programs, whereby these cars are sold as “almost new” (usually less than one year old, that is why the term therefore is in German “Jahreswagen”), creating another market for the OEM.[58]

It is really difficult to define measurable factors for brand building and somewhat easier for sales. Nevertheless I applied the following factors:

- ***Brand value***: After all, the efforts and money spent on brand building has an effect that can be measured in money – the value of the brand. Basis of this indicator is the “BrandZ Top 100 Most Valuable Global Brands 2014” study of MillwardBrown[59] and Forbes’ “The World’s Most Powerful Brands”[60] , the KPI is the brand value average from the studies in US$ (some brands were indicated only in one of the studies, there the single value were applied, the lack of presence the brand in the list is indicated with “n.a.”).
- ***Customer Satisfaction***: Measuring the customer’s satisfaction with car brands is a very subjective topic. Here again I took the help of three studies, one from the U.S., one from the U.K. and one from Germany to give an overview of the customer satisfaction of three major markets. The KPI is the average score of the three studies[61]. Two of the three studies have identical punctuation, in order to have comparable results for the third (U.S. based) study, the results were multiplied by 6.5 times[62]. Where the brand was not ranked the aggregate comes from the surveys where the brand was ranked.
- ***Sales Growth:*** Sales growth is supposed to be more dynamic at the premium brands, who manage every year to reach new records even under the fierce competition. For the KPI I took the worldwide sales of the years 2009-2013 as a basis[63].
- ***Residual value:*** One typical characteristic of a premium car ought to be that however it costs more than volume brands, it keeps its value also much better. This is a typical reason why fleet customers, who are less convinced by the brand effect, than by figures often choose premium brands. The basis for the KPI here is solely the German market and the aggregate of two forecasts of Bähr & Fess for the residual value of a 4-year-old car in 2014 (purchased in

[57] Nevertheless BTO and BTS is practiced parallel by several volume brands in Europe, but Asian and Amercian volume brands have typically BTS strategy.

[58] in. Rosengarten and Stürmer, 2011 p. 34

[59] MillwardBrown is a leading firm in marketing, advertising and market research. Their 2014 study rates the 100 global brands, as well as the top 10 car brands (where only 6 of the 10 are part of the top 100 global elite club). *BrandZ Top 100 Most Valuable Global Brands 2014, p. 26-29, 60-63.*

[60] According to the Methodology Article of Mr. Kurt *Badenhausen* on the applied methodology, the study was made in 2013. *http://www.forbes.com/powerful-brands/list/*

[61] The three studies are: „Best Car Brand Perception survey“, U.S. (2014, made by consumerreport.org), UK Vehicle Ownership Satisfaction Study (2013) and Germany Vehicle Ownership Satisfaction Study (2013, both made by JD Power and Associates). All the studies are accessible at *http://www.rankingthebrands.com*.

[62] Example: First in the U.K. study was Jaguar with 827 points, and Chevrolet is 27th with 691 points, while in the U.S. study, the first is Toyota with 145 points and Nr. 10 is BMW with 73 points. By multiplying the U.S. study by 6.5, the result is 942 points for Toyota and 475 for BMW – not exactly on the same scale, but it is enough for a comparison with a weight of 1/3 of the total.

[63] Based on respective annual reports of 2009 and 2013.

2010), respectively in 2017 (purchased in 2013)[64]. Eight categories were observed, where volume and premium play more or less in the "same league": small cars (B-segment), compacts (C-segment), mid-size (D-segment) and upper mid-size (E-segment), as well as mini-compact and full size SUVs. Below these categories premium players are hardly present, above these categories (luxury cars, SUV, sport cars, etc.) volume brands are either not present or have a tremendous loss of value which hinders a fair comparison. In the study, the top 3 models with the biggest percentile residual value in the respective categories is listed. The KPI is added up as follows: a rank 3 within a category is worth 1 point, 2nd place 2 points and for 1st place the brand receives 3 points and then the average for the two forecasts is counted. The positions for this KPI volume and premium is not consisting of the average of the three-three brands, but of the sum of the results of all volume and premium brands in the study.

- ***Leasing rates:*** leasing rates give also a good overview on the value loss of a car. For the example I took the leasing offer of Sixt Germany. Similar conditions were applied – compact car with basic trim, 36 months leasing with 10,000 km/year mileage[65].

Differentiation categories		Volume Brands				Premium Brands			
		Volkswagen	Renault	Ford	Volume Avg.	Audi	BMW	Porsche	Premium Avg.
Brand Building and Sales	2014 Brand value in $	8.3 bn.	n.a.	11.2 bn.	***9.75 bn.***	9 bn.	26.8 bn.	5.7 bn.	***13.8 bn.***
	Customer Satisfaction (agg. points in studies)[66]	793	772	775	***780***	787	683	n.a.	***735***
	Global Sales Growth 2009-2013 (in %)	32.5%	12.7%	29%	***24.7%***	39.9%	34.5%	53.9%	***42.8%***
	Residual value of a typical vehicle (scored points)[67]	5	1.5	0	***13.5***	5.5	9.5	2.5	***26.5***
	Leasing rate of a typical vehicle (in %of list price / month)	1.08%	0.99%	0.69%	***0.92%***	1.11%	1.01%	1.33%	***1.1%***

Figure 2-5: brand building and sales

The Results shown in Figure 2-5 give a more complicate picture. It is really hard to measure the brand's value and results show, that big volume brands can be just as

[64] Source: *http://www.focus.de/auto/ratgeber/kosten/tid-20070/gebrauchtwagenpreise-der-zukunft-die-restwertriesen-2014-die-neuwagen-mit-dem-geringsten-wertverlust_aid_559341.html*, and *http://www.focus.de/auto/ratgeber/kosten/tid-34681/restwertriesen-2017-2-die-neuwagen-mit-geringsten-wertverlust_aid_1158978.html*

[65] The observed car types were: VW Golf, Renault Megane, Ford Focus, Audi A3, BMW 1-series, and Porsche Boxster - basic trim (2-3-doors), basic petrol engine. Source: *http://www.sixt-neuwagen.de/leasing/*

[66] If the index is based only on the U.K. and German studies (without the U.S. study which has a distorting effect) volume average is 779 and premium average is 787.

[67] Results of MINI are accounted to BMW's results. Since the basis is the German market, German brands have better results. The compact and mini-SUV category is dominated by volume brands, the small car, compact SUV and SUV segments are mixed, while at the mid-size and upper mid-size segments only premium brands are present in the top 3.

worthy as the most respected premium brands (the premium average is greatly influenced by BMW’s value of over $26 bn., and even this value is not enough for the top of the automotive brands – another traditional volume brand, Toyota has a value of almost $30 bn., while the most valuable brand overall is Google with $159 bn.). Also customer satisfaction shows, that customers of volume brands are similarly satisfied with their cars, as premium customers (who have of course higher expectations for the higher price). Sales growth shows that premium brands clearly excess volume brands in the global growth. Finally, residual value and leasing rates are for the first glance contradictive: premium brands indeed keep their value better, but in the compact class, volume brands (basis of the analyzed leasing rates) can keep up with the competition – Porsche was here an exception, hence Boxster is the smallest within the brand, but being a sports car costs three times as much as the observed compact cars and has a proportionally bigger value loss as well.

2.5 Financial results

How easy has the CFO of a premium company? How does the premium product contribute to the company’s financials?

1.) The price premium
The basic differentiator regarding financial results is the premium price (or in another way formulated the price premium). The main issue is not revenue, but profit. By selling cars with premium price and in the price range, where volume brands do not stand a chance, from the financial point of view the main goal must be, to keep the costs down, not to consume the profit reached with the price premium. Therefore a higher EBIT margin, proportionally higher profit is possible[68].

2.) financial power from own funds
The higher price enables real earning power for the premium companies. This can enable to run the business from own funds, with less liabilities, bonds or credits than volume players.

Accordingly the following factors have been compared:

- ***Model price range***: The results shall give an answer to the real price difference between volume and premium[69][70].
- ***EBIT***: Do premium players deliver more profit[71]?
- ***EBIT margin***: Since volume companies are usually way larger than the premium ones, the EBIT margin gives the real comparison, how more profitable premium brands are.

[68] EBIT Margin: EBIT / Revenue * 100
[69] Calculated from the domestic market models on 30/04/2013 (VW: Polo vs. Phaeton, Renault: Twingo vs. Grand Espace, Ford: Fiesta vs. Expedition, Audi: A1 vs. R8 Spyder, BMW: 1 series vs. M6 Cabriolet, Porsche: Boxster vs. 918 Spyder)
[70] Ford Motor Company data calculated from USD to EUR at the conversion rate valid on 31/12/2013 (0.7255 €/$)
[71] Volkswagen and BMW data correspond to group results both at EBIT and EBIT growth. BMW and FORD data contains only the automotive division.

Differentiation categories		Volume Brands				Premium Brands			
		Volkswagen	Renault	Ford	Volume Avg.	Audi	BMW	Porsche	Premium Avg.
Financial Results	Model price range	€9,975 - €104,075	€13,900 – €54,000	€10,230 – €37,504	***€11,370 - €62,9310***	€16,750 – €127,000	€21,950 – €131,400	€49,957 – €839,000	***€29,550 - €395,830***
	EBIT as of 31/12/2013 (€)	12.43 bn.	1.13 bn.	3.87 bn.	***5.81 bn.***	5.32 bn.	6.56 bn.	2.58 bn.	***4.82 bn.***
	EBIT margin as of 31/12/2013	5.9%	1.0%	3.9%	***3.6%***	10.7%	10.5%	18.0%	***13.1%***

Figure 2-6: Financial KPIs

The figures show that there is a major difference in the price range (even if Porsche's results distort the results somewhat – Audi's and BMW's prices give rather the upper average). EBIT and EBIT margin show that volume companies play in another league with respect to sales volume and are also profitable, but their margin is $^{1}/_{3}$ – ¼ of the premium brands.

2.6 Production

Lean production introduced by Toyota in the 1960's was really the "Machine that Changed the World". The Toyota Production System (or TPS) serving as a basis of lean production is usually considered as a next evolutionary step in industry after the age of mass production (with its pike time in the 1950's America with Ford's factory practices and GM's marketing and management techniques and mix in organized labor's new role in controlling job assignments and work tasks)[72]. In the post war industrial Japan a very different approach to production was developed: Very roughly formulated the essence of lean production is to avoid waste (in Japanese "muda") and concentrate only on the activities that add value[73]. This was supplemented by the operation management checklist, the 5Ss – the 5Ss are not only a checklist, but also an easy vehicle with which to assist the culture change that is often necessary to bring about lean operations[74]. Starting with the Japanese volume players, lean production became a standard at all automotive companies, also at the premium brands, but lean in the premium world has other implications, than in volume production – the emphasis is in the case of premium companies on managing the complexity in a lean way.

Just-in-Time or JIT[75] deliveries were also introduced parallel with the lean operations and contributed to a slim lean production/inventory.

The essence of Toyota's lean production is to stay slim, and concentrate on as effective production as possible. This means also, that variations within a model are

[72] in: Womack, p. 41
[73] The 8 types of waste are: Overproduction, Queues, Transportation, Inventory, (unnecessary) Motion, Overprocessing and Defective Poducts.
[74] in: Heizer, p. 655. The 5Ss are: Sort/Segregate, Simplify/straighten, Shine/sweep, Stanardize and Sustain/selfdiscipline.
[75] Heizer defines JIT as Continous and forced prolem solving via focus on throughput and reduced inventory. in: Heizer, p. 654

considered as unnecessary complications which result in higher production costs, stock and higher possibility of failure (this concept was only strengthened by the fact that the customers of Japan's Nr. 1 export market, the U.S. did not require long lists of extra features, and anyhow it would have been troublesome for Japanese manufacturers to build-to-order, if they had to ship the ready cars over the Pacific).
Seeing the success of it, all the automotive companies took over the concept of lean management (today, beside the Toyota Production System, also Ford Production System, Volkswagen Production System, Audi Production System, etc. exist – all based on lean management principles), but premium brands had to implement it in another way – for premium brands, lean management is a tool to cope with the tremendous complexity.

Also, actual data shows that premium players have the utilization of their production capacities on a higher level than volume brands (s. figure 2-7):

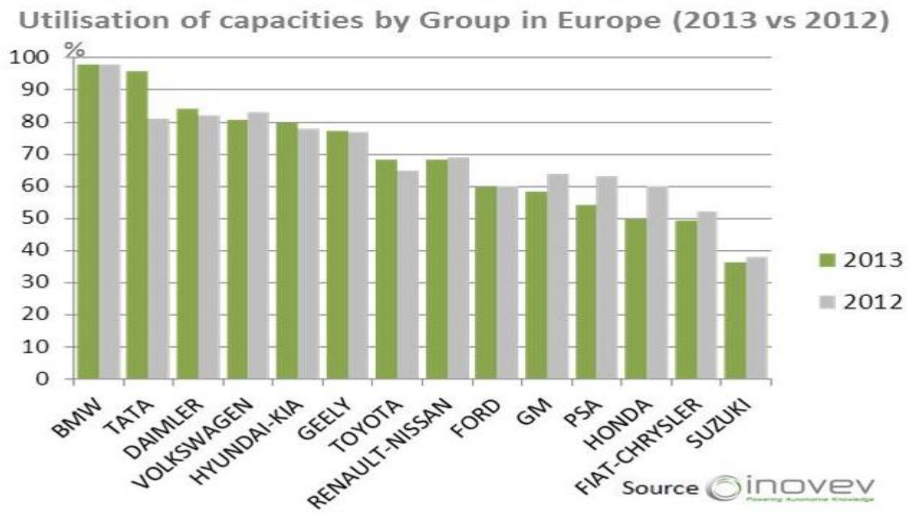

Figure 2-7: Utilisation of capacities by Gorup in Europe (2013 vs. 2012) (source: INOVEV, 2014[76])

Some key factors with regard to production are as follows:

1.) Managing complexity
What do we mean under complexity in terms of production? Why should a sophisticated Toyota Prius be less complex, than a Mercedes-Benz E-Class? As described above, Japanese car manufacturers stay lean also because of the fewer variations of their cars (usually there are only 2-3 trims per model and of course different colors, but no long list of extra features), but premium brands concentrate on serving the individual needs of their customers (an example: BMW's 1 series has only with regard to the colors-upholstery-bars-rim 6,516 combinations – with the possible combinations of extra features, engines and chasses the possible combinations reach easily millions)[77].

So the complexity is not (only) the applied technology itself, but the variations, which must be considered, kept and managed through the whole production process (including the whole supply chain) and of course to manage not only the variations

[76] Source: *http://www.inovev.com/index.php/de/analyses-list/1377-2014-10-9*
[77] in: BMW 1 series Official Product Information; *www.bmw-mail.com/ics/downloads/Der_neue_BMW_1er.pdf*

for the given car but to order/store (or when staying lean – keeps stores low of) several variations for the same part/module as well (like different seat modules). Complexity is further rising through requirements derived of deliveries for a global market (a very classic example is steering on the left or the right sides, but major markets have several – not necessarily synchronized provisions), or the individual programs of the premium brand (like custom made colors).

2.) Importance of JIS/JIT

Just-in-Time is a great tool to reduce inventory in classical lean production, Just-in-Sequence, or JIS is the solution of logistics managers to cope with supplies whereby the same part or module itself has several variations. Typical example for JIS-deliveries are seats or front-ends. At JIS deliveries, the supplier is sorting the parts before delivery to the plant. This enables delivery of the part directly to the assembly line in the desired sequence without stocks.

3.) Flexibility of the production

The BTO strategy of premium brands affect the stocks on the fully-built-unit (FBU) side. Since the manufactured cars already have their designated owners, premium brands do not keep stocks of ready cars (this is a bit different for example on the U.S. market and China, where even the European premium brands build up stocks because of the local customer habits).

Flexibility means also, that premium brands usually build cars not only with millions of possible variations, but are able to build several different models on a single assembly line. Premium brands also focus more on capacity utilization, since their models are produced in smaller numbers at the same time – this is a good way to avoid overcapacity but may cause longer waiting times for the BTO vehicles[78].

4.) Emphasis on production in the domestic area

Premium brands have their core capacities where their roots are. For example BMW's three core manufacturing sites (Munich, Dingolfing and Regensburg) are planned close to each other (making the change in the workforce even more flexible), but this has to do a lot with the brands own DNA as well (Made in U.S.A., Made in Germany, etc)[79].

With regard to production, there are plenty of KPIs for the analysis, but good KPIs to compare volume and premium brands are harder to find. The following factors were analyzed:

- ***Capacity utilization:*** The KPI shows, the capacity utilization of the car makers based on figure 2-7. Note: Only group wide European data was accessible, which means that only Ford Europe is considered, while VW accounting for the whole group including Audi and Porsche, therefore Audi and Porsche data is marked with "n.a.".
- **Flexibility**: this indicators ought to show, how the car makers can cope with the complexity of producing several models. Due to the lack of accessible information in this regard, the KPI is based on how many different models/derivates can be produced on one single plant (no data was accessible for models on one single assembly line which could give a more precise approach to the thesis of premium brands better coping with

[78] in: Rosengarten and Stürmer, p. 192

[79] An interesting example is the Porsche Chayenne almost completely manufactured in Bratislava, Slovakia, and then transpoprted to Leipzig for the final assembly. The result: „made in Germany".

complexity). The chosen plants – with most models produced by the given brands – are Wolfsburg/Germany for VW, Sandouville/France for Renault, Genk/Belgium for Ford (to be closed in 2014), Ingolstadt/Germany for Audi, Regensburg/Germany for BMW and Zuffenhausen/Germany for Porsche[80].

- ***Production volume /Staff***: This ratio shows, how many cars are produced by a single employee (of course, non-production employees are also considered), a good measure with regard to lean production.
- ***Domestic production ratio***: This ratio shows, how international is the production of the brand, or how important the domestic country is for the production.

Differentiation categories		Volume Brands				Premium Brands			
		Volkswagen	Renault	Ford	Volume Avg.	Audi	BMW	Porsche	Premium Avg.
Production	Capacity Utilization (2013, in %)	81%	68%	60%	***69.67%***	n.a.	97%	n.a.	***n.a.***
	Flexibility (Nr. of built derivates in the plant)	4	3	3	***3.33***	15	8	4	***9***
	Production volume/Staff	55.11	17.50	37.02	***36.54***	22.01	19.51	8.48	***16.67***
	domestic production ratio	24%	n.a.	49%[81]	***36%***	53%	65%	100%	***73%***

Figure 2-8: Production KPIs

The above KPIs show a clear difference between volume and premium. Premium brands have better capacity utilization (although only BMW is within the KPIs, Daimler also has a capacity utilization of around 85% - this has to do primarily with the greater demand for premium cars) and flexibility (figure 2-4 showed that premium brands have significantly more models/derivates which have to be produced in the – relatively – few plants of these players). Volume players can stay of course leaner (greater number of produced cars per employee) and are more globally established (domestic production ration is lower than at the premium brands).

2.7 General Organization and Human Resources

Premium and mass brands need a completely different way of organization. Organization of a premium brand is characterized by a high vertical depth of integration – this means for all a combination of the relevant value added stages of business (development, production and sales) a unitary management. The vertical integration is also essential in order to ensure the brand identity.[82]

Also being premium is only possible by training, hiring and keeping the best heads from the industry – this is a great challenge for the HR departments in every automotive company, for all in the times, when cars are more about electronics, than

[80] The KPIs are based on the German article by "Auto Motor und Sport". Only European Ford plants are considered. source: *http://www.auto-motor-und-sport.de/bilder/die-autoproduktionsstandorte-wer-baut-welches-auto-wo-3969472.html*

[81] Data only of North America region available (incl. U.S. and Canada assambly plants)

[82] in: Gottschalk, p. 139

mechanics, and the employers are not only competing with each other but also with the "e-giants", as Apple, Google, Samsung or SAP.

What can be relevant characteristics for the premium brands?

1.) Brand independence
As described above, it is essential for a premium brand to ensure brand identity. Premium brands need their independence in order to keep and develop their brand DNA and stay flexible.
The other way is a kind of lean strategy, to keep all functions centralized in order to gain the utmost synergies in R&D, finance, workforce-management, etc.[83]

2.) Separate and own Organization
Successful premium brands usually have – resulting from the above described brand independence – their own organization, e.g. own R&D and sales division. The reason is again the same – effectively through decisions on the premium brand's level.

3.) Premium brands also use synergies
In the automotive industry, economies of scale is a great advantage in today's times when R&D costs rise while the life-cycle of a model shrinks. There are hardly any premium brands which can afford to stand alone – in this case, it is vital to share development costs. These synergies can easily come from the group which the premium brand belongs to. A very typical example is Audi, which profits greatly as part of the VW Group[84]. Cadillac as a brand uses GM's toolkits, or Lincoln of Ford. Mercedes-Benz and BMW are exceptions in this regard, namely they are the leading brands of their respective group, but the core brand Mercedes-Benz or BMW gives the overwhelming majority of the group's production volume. Both brands tried – unsuccessfully - to solve this problem by building up their own wide product portfolio[85], nowadays a new strategy is the cooperation with groups who are not direct competitors[86].

4.) Premium brands stay also for premium working environment
Premium brands are typically top employers in the countries in which they are present[87]. The premium brands concentrate on hiring good employees and keeping the gained knowledge – for engineers working at an innovative premium car manufacturer is a benefit of its own. This strategy can be costly at times of economic depression but results in better position for the future[88].

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83 This was a typical approach of the Detroit big three in the 20th century: GM, Ford and Chrysler managed a diverse brand-portfolio, but most functions were centralized, which resulted in some models, which were 99.9% alike with models of other brands of the group just offering a different trim (e.g. Chrysler Voyager – Plymouth Voyager – Dodge Caravan in the 1980s-1990s).

84 Volkswagen's modular construction kit strategy has two major technology platforms: the Modular Crosswise Construction Kit ("MQB") for smaller cars, where VW is in charge of the development and the Modular Longitudinal Construction Kit ("MLB") for bigger cars, the natural market of Audi, whereby Audi is in charge of development but they both have access to the technology.

85 See Daimler's adventure with Chrysler or BMW's acquisition of Rover.

86 E.g. Cooperation of Daimler with Renault, or BMW with PSA

87 Again a German example: In the 2013 study of the "Focus" magazine all the four German premium brands are within the top 10 employers (BMW – Nr.2, Audi – Nr.3, Porsche - Nr. 4, Daimler – Nr. 8) – source: *http://www.focus.de/finanzen/news/unternehmen/tid-30114/grosse-focus-studie-deutschlands-beliebteste-arbeitgeber-diese-firmen-sind-die-besten_aid_940347.html*

88 A Hungarian example for the investment in employees: 2009 and the economic crisis hit both Audi Hungary and Suzuki's Esztergom plant. Audi managed to keep its personal with special measures

The following categories have been further analyzed with regard to general organization & HR:

- ***Brand independence***: How independent is the brand within the group? An answer for this question can deliver whether the observed brand is a separate legal entity within the automotive group. One example is Audi, whereby – even at an ownership rate of more than 99% - the company is a separate legal entity, a full function company, on the other hand for example General Motors is not splitting its organizations in brands (Chevrolet or Cadillac are only brands, not separate entities). Taking a premium/volume average does not really make sense in this case and was accordingly marked with "n.a.".
- ***Organization of the brand***: What are the main Directorial (top management) levels, if the brand is within the group company, who is responsible for the brand? Taking a premium/volume average does not really make sense in this case and was accordingly marked with "n.a.".
- ***Group Synergies***: Standing alone can be very costly, therefore it is essential for premium brands (with less volume) even more than volume brands to use the resources as effective as possible. The table shows the ratio between the brand's sales volume and the parent (group) company's sales volume. A lower ratio shows that the brand can better profit from the group synergies.
- ***Staff effectiveness***: Regarding human resources, it is really interesting to see how much staff is needed for a premium and how much for a volume brand to produce a car or reach a profit of one euro.

Differentiation categories		Volume Brands				Premium Brands			
		Volkswagen	Renault	Ford	Volume Avg.	Audi	BMW	Porsche	Premium Avg.
General Organization & HR	Brand is a separate company or part of the group company	Not a separate company	Not a separate company	Not a separate company	*n.a.*	Separate company	Not a separate company	Separate company	*n.a.*
	Brand organization	8 responsible for the brand	10 (board of mgmt) + 18 (senior manager) make up the mgmt. commitee	18	*n.a.*	7	8 (responsible for brand and group)	7	*n.a.*
	Group synergies	61.0%	25.7%	n.a.[89]	**43.3%**	16.2%	84.3%	1.7%	34.1%
	EBIT / Staff	26 859 €	9 261 €	22 614 €	19 578 €	74 115 €	65 157 €	132 580 €	90 617 €

Figure 2-9: General Organization & HR strategies

The table shows, that volume brands are usually not a separate legal entity, they are in most cases the leading brand within the group but lack the independence compared to the most successful premium brands. BMW is in this regard and also for group synergy an exception – this is due to the fact that the brand BMW is the leading brand of the BMW Group, and the BMW brand itself is responsible for more than 80% of the group's total car production (otherwise it is clear the premium brands

like insourcing, Suzuki sacked over 1,000 employees. After the crisis gone Audi had better chances to keep high quality and production with its original staff.

[89] No publication from Ford on division of production per brand could be found, therefore I disregarded Ford in this aspect. Nevertheless based on Ford's „One Ford" strategy, the cars under the brand „Ford" are probably above 90% of the group's total production volume.

not standing alone can profit from the group synergies at most – but this is true also for Renault, who has great benefits with the alliance with Nissan). Brand organization shows also that premium brands have a leaner management, than big leading volume brands (again: we must highlight BMW with 8 board members for the group level). The staff effectiveness shows undoubtedly, that premium brands gain over proportional profit per employee.

2.8 Summary

In Chapter 2, there were a couple of factors identified, which are – usually – quite different at a premium brand, but even within the premium brands

2.8.1. Summary of the main factors to be observed in Chapter 3

The following factors were identified on the fields of:

Innovation:

1. Importance of R&D
2. Investing in innovation
3. Eagerly searching for new segments
4. Cooperation within the automotive industry
5. Inter-industrial cooperation
6. Key R&D fields must stay in-house

Brand building and sales:

1. Transfer of innovation-primacy to the brand
2. Brand history and the Premium heritage
3. Sponsoring
4. Image transfer from and to other brands and products
5. Pricing and trims
6. High residual value
7. Customers and markets

Financial results:

1. Price premium
2. Financial power from own funds

Production:

1. Managing complexity
2. Importance of JIS/JIT
3. Flexibility of the production
4. Emphasis on production in the domestic area.

General Organization &HR:

1. Brand independence
2. Separate and own Organization
3. Premium brands also use synergies
4. Premium brands stays also for premium working environment

2.8.2. Summary chart of the gathered data

Differentiation categories		Volume Brands				Premium Brands			
		Volkswagen	Renault	Ford	Volume Avg.	Audi	BMW	Porsche	Premium Avg.
Innovation	Expenditure on R&D / total revenue (in %, as of 31/12/2013)	5,80%	4,43%	4,59%	***4,94%***	7,95%	6,30%	11,17%	***8,47%***
Innovation	Number of derivates	24	27	17	***22,67***	48	39	7	***31,33***
Innovation	Number of patent applications in 2013	40	48	22	**37**	132	67	24	***74***
Innovation	Total Number of patent applications as of 30/04/2014	110	401	129	**213**	325	427	249	***334***
Brand Building and Sales	2014 Brand value in $	8.3 bn.	n.a.	11.2 bn.	***9.75 bn.***	9 bn.	26.8 bn.	5.7 bn.	***13.8 bn.***
Brand Building and Sales	Customer Satisfaction (agg. points in studies)	793	772	775	***780***	787	683	n.a.	***735***
Brand Building and Sales	Global Sales Growth 2009-2013 (in %)	32.5%	12.7%	29%	***24.7%***	39.9%	34.5%	53.9%	***42.8%***
Brand Building and Sales	Residual value of a typical vehicle	5	1.5	0	***13.5***	5.5	9.5	2.5	***26.5***
Brand Building and Sales	Leasing rate of a typical vehicle (in %of list price / month)	1.08%	0.99%	0.69%	***0.92%***	1.11%	1.01%	1.33%	***1.1%***
Financial Results	Model price range	€9,975 - €104,075	€13,900 – €54,000	€10,230 – €37,504	***€11,370 - €62,930***	€16,750 – €127,000	€21,950 – €131,400	€49,957 – €839,000	***€29,550 - €395,830***
Financial Results	EBIT as of 31/12/2013 (€)	12.43 bn.	1.13 bn.	3.87 bn.	***5.81 bn.***	5.32 bn.	6.56 bn.	2.58 bn.	***4.82 bn.***
Financial Results	EBIT margin as of 31/12/2013	5.9%	1.0%	3.9%	***3.6%***	10.7%	10.5%	18.0%	***13.1%***
Production	Capacity Utilization (2013, in %)	81%	68%	60%	***69.67%***	n.a.	97%	n.a.	***n.a.***
Production	Flexibility (Nr. of built derivates in the plant)	4	3	3	***3.33***	15	8	4	***9***
Production	Production volume/Staff	55.11	17.50	37.02	***36.54***	22.01	19.51	8.48	***16.67***
Production	domestic production ratio	24%	n.a.	49%	***36%***	53%	65%	100%	***73%***
General Organization & HR	Brand is a separate company or part of the group company	Not a separate company	Not a separate company	Not a separate company	***n.a.***	Separate company	Not a separate company	Separate company	***n.a.***
General Organization & HR	Brand oganisation	8 responsible for the brand	10 (board of mgmt) + 18 (senior manager) make up the mgmt. commitee	18	***n.a.***	7	8 (responsible for brand and group)	7	***n.a.***
General Organization & HR	Group synergies	61.0%	25.7%	n.a.	**43.3%**	16.2%	84.3%	1.7%	34.1%
General Organization & HR	EBIT / Staff	26 859 €	9 261 €	22 614 €	19 578 €	74 115 €	65 157 €	132 580 €	90 617 €

figure 2-10: Summary chart of chapter 2

The above summary chart gives a rough overview of the different KPIs, which have been discussed in details in the previous chapters. As multiple times emphasized before the comparison is not all the time exact and not all KPIs give a precise picture of the difference in the business models “volume” and “premium” but it gives at least an overall comparison and a basic idea behind the different business models.

Some of the different characteristics must be highlighted, which show the significant difference:

- It is clear from the sheet, that premium brands spend on the average about double the ratio to their revenue amount on R&D (4.94% vs. 8.45%) – this is the basic difference related to innovation supremacy of premium brands.
- Trend in the past years on the “old” (TRIAD) markets as well as on the “new” (BRIC) markets is the shift towards premium brands (sales growth of 24.7% vs. 42.8%). This clearly shows the importance of having a premium brand strategy, respectively having a successful strategy.
- Price range and EBIT margin clearly indicates the other, even more important criteria for shareholders, expensive products (range between the cheapest models is 3 times, between the most expensive 5 times) and a profit margin that is 4 times greater than of volume brands (3.6% vs. 13.1%)!
- The more effective way of producing profit is also clearly indicated in the EBIT/Staff KPI (~20,000 EUR vs. ~90,000 EUR profit/employee, again a difference of 4.5 times).
- Premium brands are more desired and their production is organized in a way that enables profitable utilization of the capacities[90], even if they need more staff to reach the same number of produced cars.

The above KPIs give an idea why it is worth for all major automotive brands to invest in their premium brands or to develop a premium brand. The idea is clear: this is the way to reach extra profits with a slim staff by delivering innovative products and build a successful and worthy brand.

[90] „If the plants reach 90% utilization, good monay is made. If the rate goes inbetween 60 an 70% enterprises lose a way lot of money” – John Hoffecker, director of Alix Partners, in: Wall Street Journal, 17/06/2013, source: *http://www.wsj.de/article/SB10001424127887324520904578550950726667488.html*

Chapter 3: Best practice in Premium Brand Strategy:

3.1. Three successful brands – thee different ways of best practice in the premium automotive business.

In Chapter 3 I will examine three different brands with three different approaches. A traditional luxury, nowadays premium brand, (Mercedes-Benz), Audi - Volkswagen's high flyer, who managed to become an equal competitor to Mercedes and BMW since the beginning of the 70's and BMW Group's MINI brand, a real jewel mined and polished from the wrecks of the Rover group, BMW's unsuccessful try to revitalize a British mass producer.

In this part I will first give a rough overview from the history of the brands and then examine the factors set forth in Chapter 2, and inter alia give an impression, how the various KPIs differ by these premium brands, if compared to the volume and premium average factors and also to each other.

3.2. Mercedes-Benz

3.2.1 The inventor of the automobile – the short history of Mercedes-Benz[91]

Karl Benz (1844-1929) developed its first petrol engine in 1879. The successful 1-cylinder engine was the basis for the development of a vehicle powered by a gasoline engine whereby the chassis and the engine is one unit. As Benz has found no solution for the steering of a four-wheeled vehicle at that time, for the time being he concentrated on building a three-wheeled vehicle, the so called "Velocipede" which was built in 1886 and which can be regarded as the world's first automobile, despite being limited to three wheels – The "Benz Patent-Motorwagen" (patented on 29 January 1886) is considered the first automobile in the world.

In the same year, just 100 kilometres away Daimler presented his motor carriage, considered the world's first four-wheeled automobile. Essentially, this automobile was a light coach in which a modified and more powerful version of the "grandfather clock" was installed. Having recognized other areas of application for his engines at an early stage, in 1886 Daimler was already giving thought to motorising boats, rail vehicles and aircraft. The brand name "Mercedes" can be connected to Daimler, or to be more particular to its first major customer, Mr. Emil Jelllinek, who ordered 36 Daimler automobiles in 1900 and gave the name of his daughter "Mercedes" to the cars. The Daimler-Motoren-Gesellschaft (DMG) produced its first Mercedes race car in December, 1900. The Mercedes-Simpley has 35 HP from a 5.9 litres engine, which enabled an unbelievable top speed of 100 km/h of its time.

[91] Chapter based on the following literature: Rosengarten p. 72 – 80; J. Hubber: Mercedes-Benz – Der Stern am Automobilhimmel (in. Gottschalk p. 323-343) and Daimler's „Company History" (*http://www.daimler.com/dccom/0-5-1324832-1-1345592-1-0-0-1345593-0-0-135-0-0-0-0-0-0-0-0.html*)

Benz was a strong competitor of Daimler's Mercedes cars until the 20's, when due to the crisis, under the main shareholder Deutsche Bank decided to merge Daimler and Benz in 1926 into the Daimler-Benz AG.
Until World War II Mercedes-Benz cars were among the finest luxury of German car-making, examples therefore are the legendary types S, SS, SSK, and SSKL winning lots of different races during the 1920's. Also in these years, Daimler-Benz has a head of the construction office who will have great impact on the post war German car industry, Ferdinand Porsche. The 1930's is the time when Nazi Germany supported overwhelmingly the racing activities of the German brands, in order to display the superiority of German car making to the world (the "silver arrows" of Mercedes-Benz and Auto Union[92]).

The destruction of the war hit also Daimler-Benz and its plants badly. Nevertheless Mercedes's post war revival was one of the best examples of the German economic miracle. In this period the production of luxury cars was first on hold (production of passenger cars ceased anyway during the war) – the first model was the 170V in the post-war period – definitely not a luxury car. The main focus of passenger vehicle production was first the reliable cars for rural Germany. The company gradually pressed ahead with expansion of the European sales network in the period thereafter. During this time, for its renewed internationalisation Daimler Benz relied almost exclusively on successes in motorsport which would refresh memories of the name Mercedes-Benz all over the world (successes in motorsport events, such as the Carrera Panamericana Mexico and Grand Prix racing). Export was the priority of sales at that time and the most attractive export market was America, where Daimler-Benz of North America Inc. was set up in 1955. The breakthrough in the US market was achieved together with American car dealer Maximilian E. Hoffmann. The 300 SL Gullwing and the 190 SL were successfully launched on the American market with his help.

Mercedes began producing again exclusive models like the mentioned 300SL or the Mercedes 300 (Adenauer Mercedes) which were symbols of the reconstruction and the economic success of their owners.

Mercedes went on the expansion course – not harmed by the oil crisis of 1973 – and investing a lot in innovation it extended its portfolio upwards (the S-class (W116) as a successor of the W108/109 series in 1972) as well as downwards.

Since Mercedes-Benz traditionally had models in the upper class, downsizing and creating the "Baby-Benz" (W201 or 190-class) was a much more risky and major step for Mercedes-Benz to become a modern premium car manufacturer. The goal was to extend the product portfolio with a segment of potential, reach younger customers, provide state of the art technology without any compromise regarding comfort, quality or traditional values. The 190-series became a great success (1.88 million units sold in 10 years) and opened the door for the expansion of Mercedes-Benz into other (partially brand new) niche categories.

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[92] The silver arrow legend's roots are the regulations based on the international automobile sport authority's initiative to limit the always stronger and heavier race cars to a limit weight of 750kg. Daimler's Type W25 was at its first race on the Nürburgring still one kilo too heavy. On 3 June 1934 Race manager Alfred Neubauer ordered to wipe off the white paint of the aluminum chassis, which not only helped to reach the race weight, but also gave a spectacular look to Mercedes-Benz race cars.

Another big step was the A-Class in 1997, again downgrading, with some spectacular features: the “sandwich-base” enabled the VW Polo size small car to provide the comfort of a C-Class. But this enter into a new segment was not as triumphant as the 190 series in the 1980’s. The famous “moose test” in Sweden raised concerns regarding the stability of the model, which was corrected in record time by Mercedes by equipping all models with the new Bosch invention Electronic Stability Program (ESP) even in the baseline trim. The A-Class had also other weaknesses which are remarkable of the era – quality issues[93].

In the 90’s Daimler had begun an exciting joint venture project with SMH, the company manufacturing and marketing the well known design watcher “Swatch”. The joint venture was founded in 1994 (under the name Micro Compact Car AG). The production began in 1998 under the brand “Smart” and the first model was the City Coupé – the car as well as the used sales methods were unique at their times. Smart did not become a great economic success, but with combination of the small car as a BEV and Daimler’s car sharing program Car2Go it might become a profitable way to provide urban mobility.

Daimler had another strategic plan at the end of the 90’s. In order to be able to dispose of a greater economies of scale and get bigger market share, Daimler conducted a "Merger of Equals" with Chrysler in 1998. The master plan was a product portfolio where Chrysler’s brands stand for volume (and a significant market share in North America), while Mercedes-Benz should have stayed for premium and a strong basis for Chrysler’s expansion in Europe. Doubts were raised, whether the transaction was really a merger or an acquisition of Chrysler by Daimler. The hoped platform strategy and synergies did not bring the results[94] as planned and Daimler decided to get rid of Chrysler and sold it to Cerberus Capital Management of $6 bn. in 2007.

Mercedes managed to cope with the quality issues and carried on the diversification of the product portfolio (with more – like the CLS class – or less like the R-Class luck), but at the of the 2010’s, Mercedes was only 3rd in terms of delivered vehicles[95]. Under the leadership of CEO Dieter Zetsche, Mercedes found a new design and with the launch of the new A-Class in 2012 and already in 2013 Mercedes had better growth rate compared to Audi and BMW.[96]

3.2.2. Innovation

1. Importance of R&D

In a history of more than 100 years, it is easy to find innovations from Mercedes-Benz which establishes its position as an innovative brand in the premium class. It needs to be highlighted, that in the past the most important innovations of Mercedes-Benz

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[93] Before the facelift of 2001, the A-Class had several quality issues – rust at the doors, cooling, automatic transmission, overheating of the engines and for the era and other Mercedes-Benz models typical electronic problems. source: *www.mobile.de/modellverzeichnis/Mercedes-benz/a-klasse-tab-test-und-vergleich-w068-1997-2007.html*

[94] Chrysler made losses in 2006 of $1.6 bn.

[95] Mercedes lost its 1st place to BMW in 2005 and 2nd place to Audi in 2011

[96] In 2013 Mercedes almost reached Audi, with 1.56 million deliveries vs. 1.58 million deliveries

were regarding safety[97]. Some of the key innovations by Mercedes-Benz are as follows:

- 1886: the first automobile, the “Benz Patent-Motorwagen”;
- 1897: the boxer-engine (Benz Contramotor);
- 1936: first passenger car with a diesel engine (Mercedes-Benz 260D);
- 1959: the safety chassis with crumple zone (Mercedes-Benz 220 series)[98];
- 1978: Anti blocking system (ABS) (Mercedes-Benz W116 series);
- 1981: Airbag (Mercedes-Benz W126 series);
- 1995: Electronic stability system (ESP, Mercedes-Benz W140 series);
- 2002: PRE-SAFE, electronic safety measures before a possible crash situation (Mercedes-Benz W220 series);
- 2009: Attention Assist (Mercedes-Benz E-Class);
- 2013: Intelligent Drive (network of the existing safety assistants creating even more safety, Mercedes-Benz S-Class).

Mercedes-Benz is a traditional brand, where innovation is at high stakes – and this is a must from a brand which claims itself the inventor of the automobile. In the Daimler top management, the head of R&D is present in the board of directors and at the end of 2013, Daimler employed 21,300 men and women at its research and development units (2012: 21,100), of which 13,600 worked at the Group Research & Mercedes-Benz Cars[99], a really impressive number. Daimler is actually in need of a broad R&D facility, since – at least on the passenger car level – it is alone with two brands, Mercedes-Benz and Smart. Smart accounts for only 6-7% of Daimler’s passenger car sales, and the cars have because of their size and target customers little common with Mercedes-Benz cars, which means that Daimler can share synergy effects only with other OEMs.

2. Investing in innovation

As described before, Daimler has to invest severe amounts into innovation in order to keep its position in the premium class without being able to get use of group synergies as can for example Audi, Porsche or Lexus. But this is rather a recent problem with the rise of R&D costs and shrinking of model lifecycles[100], Daimler needs to find partners to get hold of R&D costs and still be able to be an innovative brand

As for the investment, in 2012 and 2013, Daimler invested for the R&D of Mercedes-Benz Cars as much as 3.8, resp. 3.9 billion Euros. For the period of 2014-2015 another 7.7 billion Euros is planned.

3. Eagerly searching for new segments

Mercedes-Benz was for a long time a traditional luxury brand, the suiting car for presidents, entrepreneurs or pop stars. Even in the pre-war times had Mercedes-

[97] According to Rosengarten and Stürmer, in a Design-Innovation-Sector matrix, regarding Innovation Audi stays for efficiency, BMW for sportiness, Mercedes-Benz for safety and Porsche for high-speed. in: Rosengarten, p. 153

[98] The inventor of this innovation was Daimler’s engineer with Hungarian roots, Béla Barényi)

[99] in: Daimler AG Annual Report 2013, p. 105

[100] As an example the E-Class of Mercedes-Benz: The W123 series was manufactured from 1976 to 1985 (9 years), the follower W124 from 1985 to 1995 (10 years), the W210 series from 1995 to 2002 (7 years).

Benz smaller, more affordable cars (like the 170 series), but this was not the daily business. In the post war times beside the special sport (like the 300SL) and luxury (like the 600 series) models, Mercedes' model line was made of the (with today's terms) "E-Class" and "S-Class". In 1980 it was a really wild step to enter into new market segment downwards with the "Baby-Benz" (190 series), just as unusual with the A-Class in 1994 but thereafter Mercedes-Benz's product portfolio was exponentially expanding. 1996 came the ML-Class, the first SUV, another new innovative segment was the coupe-limousine of the CLS Class in 2004, and nowadays Mercedes-Benz offers in all of four segments from A- to S-Class, limousines, SUV-s , wagons, coupes, cabriolets, coupe-limousines and so on. As of June, 2014 Mercedes-Benz has 25 derivates (with AMG versions a total of 40 models), the same magnitude, as the core competitors BMW and Audi have.

4. Cooperation within the automotive industry

As mentioned before, a cooperation with suppliers, as well as other OEMs is a must to survive in the time of ever rising R&D costs.

Mercedes-Benz has a traditionally good relationship with the big tier 1 suppliers, for all with Bosch (the partner with whom Mercedes-Benz jointly invented the ABS or the ESP).

Unlike Audi, Mercedes needs nowadays OEM partners as well and is likely to have found it with Renault[101]. The cooperation started in 2010 and was – as usual in the industry – strengthened by a mutual acquisition of share (3.1% of Daimler in both Nissan and Renault and 1.55% of Nissan and the same for Renault vis-à-vis in Daimler). The cooperation is including 10 areas, the most important, the platform-sharing of the new Smart fortwo and Renault Twingo, selling the Renault Kangoo rebranded as Mercedes, but also other plans are considered, e.g use of Mercedes components in Nissan luxury brand Infiniti's new SUV Q30 or the possible production of the Mercedes-Benz CLA-class in a Nissan plant in Mexico.[102] Another cooperation is with Aston-Martin, starting in 2013, according to which Daimler shall supply the traditional British luxury brand with engines[103].

Another interesting cooperation is with the so-called "0.5" tier supplier Magna-Steyr, who is manufacturing the G-Class, an old fashioned but still very popular jeep in Graz, Austria.

5. Inter-industrial cooperation

Beside the traditional cooperation with other premium or luxury brands from other industries (like in case of Daimler the already mentioned cooperation with Burmaster) the cooperation with the giants of the electronics industry and the platform from the onboard infotainment in cars is an up-to-date issue. Apple, Google, Blackberry's

[101] Daimler and Volkswagen have long years cooperation on the light commercial utility vehicles level (joint production of Mercedes Sprinter – VW LT/Crafter), but it is here because of the premium aspects disregarded.

[102] source: *http://www.caranddriver.com/news/daimler-and-renault-nissan-announce-global-partnership-car-news; http://www.handelsblatt.com/unternehmen/industrie/kooperation-daimler-und-renault-nissan-wahren-sicherheitsabstand/8774966.html*

[103] source: *http://www.spiegel.de/auto/aktuell/technik-kooperation-daimler-steigt-bei-aston-martin-ein-a-940118.html*

QNX, Microsoft and Nokia all offer solutions, and the time for the automotive players have come to integrate the until now only as smart phone features known software in their cars. Daimler (along with Volvo and Ferrari) was among the first to join Apple in the cooperation and will in the close future integrate Apple's software in its cars[104].

6. Key R&D fields must stay in-house

As written before, Daimler has a severe R&D department and is able to develop all components for its cars on its own.

7. Comparison of KPIs

Differentiation categories		**Volume Avg.**	**Premium Avg.**	
Innovation	Expenditure on R&D / total revenue (in %, as of 31/12/2013)	***4,94%***	***8,47%***	***6,55%***
	Number of derivates	***22,67***	***31,33***	***40***
	Number of patent applications in 2013	**37**	***74***	***107***
	Total Number of patent applications as of 30/04/2014	**213**	***334***	***562***

Figure 3-1: Innovation KPIs for Mercedes-Benz

The KPIs show that Mercedes-Benz is a successful premium brand regarding innovation. However the innovation spending is somewhat less than the premium average, Mercedes-Benz has just as many derivates as core competitors Audi or BMW and a great number of patent applications, more than the premium average.

3.2.3. Brand building and Sales

1. Transfer of innovation-primacy to the brand

Mercedes-Benz never had a problem neither with innovation, nor with strength of the brand and still it could not keep its position as the nr. 1 premium brand. There can be numerous reasons for it, beginning with the ageing of traditional Mercedes-Benz customers, to quality problems as the end of the 1990s, insufficient presence in the BRIC regions at the beginning of 2000, or not proper definitions of market core values. Regarding market core values, Kilian is in its 2009 article[105] of the opinion, that Mercedes-Benz did not apply a proper brand value definition, unlike its core competitors Audi and BMW (Audi applies the characteristics high-class, sporty and progressive with the brand value technical supremacy, while BMW applies the characteristics dynamic, cultured and challenging with the brand value pleasure) – as the inventor of passenger vehicles, Mercedes-Benz could greatly base on "inventive"

[104] in: *http://www.welt.de/wirtschaft/article125342696/Mercedes-und-Ferrari-holen-sich-Apple-ins-Auto.html*

[105] in: K. Kilian, So bringen Sie Ihre Marke auf Kurs, in. Absatzwirtschaft, 4/2009, p. 43

as a core value. Rosenberger and Stürmer believed in their 2004 book that Mercedes-Benz has a strong premium message of “exclusivity”[106].

Motorsport as brand-builder has also a century of tradition at Mercedes-Benz, beginning with the first Mercedes 35 PS as a race car in 1900, through the silver arrows during the 1930’s, the Carrera Panamericana winner 300SL in 1952 up to the 21st century, founder of the DTM series and successful engine supplier, as well as team at the king class of the motorsport, the Formula 1.

2. Brand history and the Premium heritage

The brand history of Mercedes-Benz has been detailed in section 3.2.1. The premium heritage of the brand cannot be questioned – Mercedes-Benz has been associated with luxury and high quality from the very beginnings onwards.

The brand’s DNA is defined by the long tradition and elegance. The Design-Innovation-Segment Matrix by Rosenberger and Stürmer accounts the following key elements to the Mercedes-Benz brand:

	Design	**Innovation**	**Speed** (Segment-specific for automotive)	**Message of the premium brand**
	Classic elegant	Safety	Comfort	Exclusivity

figure 3-2: DIS-Matrix for Mercedes-Benz (based on chart of Rosegarten and Strürmer)

3. Sponsoring

Mercedes-Benz, as a premium brand is historically and widely engaged on the different fields of sponsoring activity, and in the recent years it also communicates its CSR[107] activities.

Mercedes-Benz has two main fields on sports sponsoring: Golf (e.g. the PGA of America) and football (very popular and is well associated with German values – for example Mercedes-Benz is the main sponsor of the German national football team).

The brand Mercedes-Benz was also multiple times present in the film industry, as a special way of marketing new models – such movies were the Jurassic Park (ML-Class, 1996) or Men in Black 2 (E-Class, 2001).

Further to the classical marketing-based sponsoring activities, according to the 2013 annual report, Daimler spent more than €60 million on donations to nonprofit institutions and sponsorships of socially beneficial projects in 2013.

4. Image transfer from and to other brands and products

Mercedes-Benz is offering under its brand fashion wear, but also supplementary functions for the navigation systems.

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[106] in: Rosenberger and Stürmer, p. 153
[107] Corporate Social Responsibility

5. Pricing and trims

The traditional premium brands, as Mercedes-Benz, Audi, BMW, but also Porsche or Jaguar are offering very similar pricing and trimming options. As of June, 2014, the prices of Merceds-Benz models cover a range of 24,400 EUR (A-Class) to 233,800 EUR (SLS AMG Roadster) at the domestic German market – quite similar to the price range average in *figure 9* (nevertheless due to the exclusive SLS AMG model the upper end is higher than at Audi and BMW but does not reach the price of the Porsche models).

As for Mercedes-Benz, for each model a wider series of extra features can be ordered, special editions are rare and usually mean a package trim. The price of a model can be easily doubled with the extra options.

Mercedes-Benz as a premium brand also avoids to build to stock or give manufacturer's discounts.

6. High residual value

The high residual value of Mercedes-Benz cars is also confirmed by the study used for figure 10[108]. As for a car bought in 2013, the following Mercedes-Benz are in the top 3 regarding the calculated residual value for a possible resale in 2017: CLA 180 (Nr. 1 at compact segment with residual value of 56%), CLS Shooting Brake 350CDI (Nr. 1 at upper middle class, with residual value of 52%) and S 400 Hybrid (Nr. 1 at luxury, with residual value of 50%) or S350 Bluetec (also Nr. 1 at luxury, with the highest nominal resale value of 40,693.- EUR) and also ML 250 Bluetec (Nr. 1 at SUV, with residual value of 54%), B 160CDI (Nr. 1 at compact van, with residual value of 56.5%), while at sports car the SLS AMG Coupé (Nr. 3, with residual value of 55%).

7. Customers and markets

The characteristics described at sub-chapter 2.4. Section 7 are true for Mercedes-Benz cars as well (BTO, strong domestic markets, "Jahreswagen" or "Junge Sterne" for Mercedes-Benz).

Regarding special (fleet) customers, Mercedes-Benz cars has strong positions at taxis all throughout Europe and upper end of state and corporate fleets all over the world.

The main markets of Mercedes-Benz were in 2013 as follows:

[108] *http://www.focus.de/auto/ratgeber/kosten/tid-34681/restwertriesen-2017-2-die-neuwagen-mit-geringsten-wertverlust_aid_1158978.html*

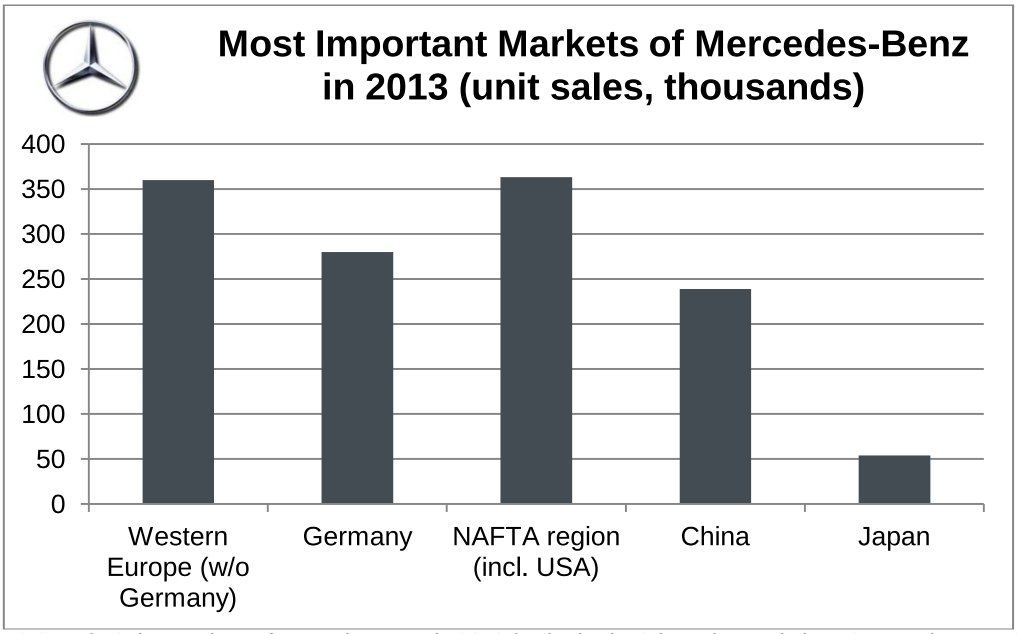

Figure 3-3: Main Sales Regions of Mercedes-Benz in 2013 (author's chart, based on Daimler AG Annual Report 2013)

According to the above chart, Mercedes-Benz has a well-established domestic market, and strong positions in Western Europe and North-America. China is not yet such a strong market for Mercedes-Benz as is for example for Audi.

8. Comparison of KPIs

Differentiation categories		Volume Avg.	Premium Avg.	
Brand Building and Sales	2014 Brand value in $	*9.75 bn.*	*13.8 bn.*	*22,5 bn.*
	Customer Satisfaction (agg. points in studies)[109]	*780*	*735*	*715*
	Global Sales Growth 2009-2013 (in %)	*24.7%*	*42.8%*	*34%*
	Residual value of a typical vehicle (scored points)	*13.5*	*26.5*	*9*
	Leasing rate of a typical vehicle (in %of list price / month)	*0.92%*	*1.1%*	*1.1%*

Figure 3-4: Brand Building and Sales KPIs for Mercedes-Benz

The above KPIs show that Mercedes-Benz is an especially strong brand even among the premium players. The brand value is one of the highest of car producers generally and Mercedes-Benz has even now a high customer satisfaction rate – the KPI can be misleading – without the American study, the rate of Mercedes-Benz is

[109] without U.S. study, the average score of Mercedes-Benz is 807

higher than the volume and also the premium average (807). However Mercedes-Benz has slightly difficult years behind itself in terms of growth compared to the arch-rivals BMW and Audi, it managed a growth in sales since the crisis of 34% below the premium average, but higher than the growth the volume brands could bring.

3.2.4. Financial results

1. Price premium

Mercedes-Benz had had difficult years behind itself, and a lot of investments to come up with fresh and successful models in the compact (A, CLA), as well as in the full size luxury segment (S).

With sales of 1.467 million cars and a revenue of € 64.31 bn., Mercedes-Benz Cars reached an EBIT of € 4 billion in 2013. Return on sales (or EBIT margin) amounted to 6.2% (1% lower, than in 2012), this is way lower, only of 60% as of Audi or BMW.

2. Financial power from own funds

Based on the annual report, we get a picture only about the liabilities of the total Daimler Group (including the quite extensive commercial vehicles segment), with a total (non-current and current) financial liabilities of € 77.7 bn.

3. Comparison of KPIs

Differentiation categories		**Volume Avg.**	**Premium Avg.**	
Financial Results	Model price range[110]	***€11,370 - €62,9310***	***€29,550 - €395,830***	***€24,400 – €233,800***
	EBIT as of 31/12/2013 (€)	***5.81 bn.***	***4.82 bn.***	***4.0 bn.***
	EBIT margin as of 31/12/2013	***3.6%***	***13.1%***	***6.2%***

Figure 3-5: Financial Results KPIs for Mercedes-Benz

Mercedes-Benz models have clearly a premium pricing strategy - as the model price range show, nevertheless the EBIT and EBIT margin is higher than the volume average but does not reach the average of the premium competitors, with the model offensive in the compact class, and the successful introduction of the new S- and C-Classes in 2013 and 2014 this is awaited to improve.

3.2.5. Production

1. Managing complexity
2. Importance of JIS/JIT

[110] German market, price of A180 vs. price of SLS AMG Roadster.

3. Flexibility of the production and
4. Emphasis on production in the domestic area.

Mercedes-Benz’s global production network must cope with the production of 40 derivates from the compact class through the large scale middle-class and upper middle-class models to the full size luxury limousines and supersport cars like the S-Class or the SLS AMG.

Mercedes-Benz’s production centers are the core plants in Untertürkheim, Stuttgart (administration, production plant for engines and components), and the closely located Sindelfingen (biggest car production plant). In Rastatt, still Baden-Württemberg, Germany are the compact cars produced in a flexible tandem with the 2008 founded production plant in Kecskemét, Hungary. Bremen is also an important production site in Northern Germany (lead plant for the large scale model C-Class).

As the premium business goes global, Mercedes-Benz cars are not only marketed but also produced throughout the globe. However, the German domestic foundations are still strong (67% of the total production in 2013), Mercedes-Benz was the first of the German premium brands to establish a plant in the U.S. (in Tuscalossa, Alabama, producing SUVs not only for the American but also the world market). Having newly established capacities the CEE Region (Hungary) and China, the production of Mercedes-Benz cars are presumably shifting also to a more global scale.

5. Comparison of KPIs

Differentiation categories		**Volume Avg.**	**Premium Avg.**	
Production	Capacity Utilization (2013, in %)	***69.67%***	***n.a.***	***84%***
	Flexibility (Nr. of built derivates in the plant)	***3.33***	***9***	***7***
	Production volume/Staff	***36.54***	***16.67***	***16.2***
	domestic production ratio	***36%***	***73%***	***67%***

Figure 3-6: Production KPIs for Mercedes-Benz

The production KPIs unanimously define the production network of Mercedes-Benz as one of the premium brands, a capacity utilization way over the volume average, production of several derivates in for example the Sindelfingen plant, less production volume per employee than the volume brands and year-to-year less, but still strong domestic foundation in the production.

3.2.6. General Organization and Human Resources

1. Brand independence

Brand independence is a special case for Mercedes-Benz, as it is a leading brand of the Daimler Group. As for passenger vehicles, Mercedes-Benz products are responsible for almost 95% of sales (in revenue even larger ratio). It can be said, that Mercedes-Benz is way the strongest brand within the Daimler Group, and gives the essence of the group spirit and DNA.

2. Separate and own Organization

For the same reason, as described at section 1, the organization of Daimler Group is focused on the Mercedes-Benz Cars segment.

Accordingly, the top management is more or less both responsible for group, as well as Mercedes-Benz Cars functions. Daimler's board of management currently consists of 8 members, Dieter Zetsche, the CEO is both responsible for the Daimler Group and Mercedes-Benz Cars. from the other 7 board members one is responsible for trucks and busses, all the other functions are joint functions for the group as well as for Mercedes-Benz Cars[111].

3. Premium brands also use synergies

Mercedes-Benz was in a special position for almost all of its history, that it stood alone as the major brand within the Daimler AG. In Daimler's recent strategy this lack of synergy effects within the group are corrected by alliances and cooperation within the industry as described at sub-chapter 3.2.2.

Daimler's CEO Jürgen Schrempp knew already in the 1990's that Daimler needs more volume and more brands in order to benefit from the synergy effects, and in 1998 the "merger of equals" (according to several experts, rather a takeover) was concluded with Chrysler and was considered as the deal of the century, with 442,000 employees worldwide, annual profits of about $130,000 billion, projected sales for 1999 of more than four million cars, expected cost-savings of about $1.4 billion in the first year and $3.5 billion within the next two or three years, and a market capitalization close to $100 billion[112]. Both companies went financially strong and with good products into the merger which nevertheless turned out to be a school-book example of unsuccessful intercultural management. Some of the reasons for the failure were for example that operations and management were not successfully integrated as "equals" because of the entirely different ways in which the Germans and Americans operated: while Daimler-Benz's culture stressed a more formal and structured management style, Chrysler favoured a more relaxed, freewheeling style. Furthermore, the two units traditionally held entirely different views on important things like pay scales and travel expenses. As a result of these differences and the German unit's increasing dominance, performance and employee satisfaction at Chrysler took a steep downturn[113]. Daimler bailed out of the mistaken alliance in 2007 by selling 80% of the Chrysler shares to a venture fond Cerberus.

[111] An interesting function well showing Daimler's drive towards the far east is the member of the board responsible for greater China.
[112] in: N. Martelin: The Daimler-Chrysler Merger Case – Rationale of a Failure, 2009, p. 9
[113] in: R.A. Weber, C.F. Camerer: Cultural Conflict and Merger Failure: An Experimental Approach, 2003, p. 2

4. Premium brands stays also for premium working environment

Daimler is among the top employers in Germany, for all in the engineering area[114] applying such up-to-date HR tools, as for example diversity management.[115]

5. Comparison of KPIs

Differentiation categories		Volume Avg.	Premium Avg.	
General Organization & HR	Brand is a separate company or part of the group company	***n.a.***	***n.a.***	*not a separate company*
	Brand organization	***n.a.***	***n.a.***	8 (responsible for brand and group)
	Group synergies	**43.3%**	34.1%	***93.6%***
	EBIT / Staff	19 578 €	90 617 €	***41,282 €***

Figure 3-7: General Organization & HR KPIs for Mercedes-Benz

As written above, just like BMW, Mercedes-Benz is a leading brand of its respective group, but possible synergy effects are here even less, because of the marginal importance of sales of smart in the Mercedes-Benz Cars group (where the brand Mercedes-Benz is responsible for more than 90% of group sales numbers and even more for group sales revenue). The financial "effectively" with ~€ 40,000 / employee is in the examined period right in-between the volume and premium figures.

3.3. Audi

3.3.1 Vorsprung durch Technik - the short history of Audi[116]

The history of Audi can only be interpreted together with the History of the Auto Union group and of a person called August Horch. August Horch founded the Horch & Cie. Motorwagen Werke in 1899 (established in Cologne, but the company moved later to Zwickau in Saxony). After having differences of opinion with the Board of Management and Supervisory Board, August Horch left the company and founded in Zwickau on 16 July 1909, the August Horch Automobilwerke GmbH. His former partners sued him for trademark infringement, which forced August Horch to change the trade name. Horch chose the Latin translation of his name for the new company.

[114] *http://www.100toparbeitgeber.de/detail/automotive/daimler/*
[115] *http://career.daimler.com/dhr/index.php?ci=988&language=1&DAIMLERHR=d02cbd84aa971263e704953938f1d15c*
[116] Chapter based on the following literature: Rosengarten p. 121-131 Gottschalk p. 155-157 *http://www.audi.com/corporate/en/company/history/companies-and-brands.html*

So "Horch!" – or "Hark!" – became "Audi!". The idea of using the Latin imperative form came from the son of one of August Horch's business partners. The brand “Horch” remained but was independent of August Horch and was manufacturing high class luxury cars – the two brands became later sister-brands within the Auto Union Group in the 1930s.
In 1910 the Audi Automobilwerke GmbH was established in Zwickau. August Horch succeeded in making Audi internationally known within just a few years with models like the Type A 10/22 hp (16 kW) Sport-Phaeton, the Type B 10/28hp or the Type C 14/35 hp (very successful on Alpine rounds and was accordingly nicknamed the "Alpine Conqueror”).

In 1932, Audi merged with Horch, DKW, and Wanderer, to form Auto Union AG, with its headquarters in Chemnitz, Saxony. Following the merger, Auto Union AG was a major player in the German automotive market. The company emblem consisted of four interlocking rings, intended to symbolize the inseparable unity of the four founder companies – also very unique in its time: the four brands formed a well-thought product portfolio: DKW stood for motorcycles and small cars (basically with two-stroke engines), Wanderer was a midsize (“value”) brand, Audi stood for midsize demands and Horch stayed for the highest luxury, a competitor of Maybach or Rolls-Royce.

It was during this period when the German car manufacturers were subsidized by the national-socialist government and which led to the famous silver arrows, the racing cars of Mercedes-Benz but also of Auto Union that overthrew several records in their times.

During World War II, Auto Union plants were involved in military production and by the end of the war the production facilities were destroyed by allied bombing raids. The restart was made even harder by the fact that Saxony was in the Soviet occupied zone, in the later German Democratic Republic.
Like most German manufacturing, at the onset of World War II the Auto Union plants were retooled for military production, and were a target for allied bombing during the war which left them damaged. The remains of the Audi plant of Zwickau became the VEB (for "People Owned Enterprise") Automobilwerk Zwickau or AWZ (Automobile Works Zwickau) and were manufacturing first pre-war DKW models and later the Trabant (based on the two-choke technology of DKW) until 1991.

The Auto Union GmbH was (re)launched on September 3, 1949 in West-Germany, in Ingolstadt, Bavaria. Production was starting also in this case with DKW models (and also under the DKW brand).
In 1958 Daimler-Benz AG gained control of Auto Union and had acquired all the shares by 1959. After DKW sales dropping a fresh new car was developed under the Daimler regime by 1965 already with a modern four-stroke engine – for this new car the brand Audi was designated, a brand with reputation from the pre-war times and the Auto Union ”Audi” became a great success.

Volkswagen acquired the majority of the shares from Daimler in 1965 and wanted to use the modern Ingolstadt plant as a mere production facility – but the Auto Union management developed an own model (against the explicit directives of

Volkswagen), which became the Audi 100, a great success and the ultimate tool to keep Audi as a separate identity.

In 1969, Auto Union merged with NSU, based in Neckarsulm, near Stuttgart and formed the Audi NSU Auto Union AG. In the 1950s, NSU had been the world's largest manufacturer of motorcycles, and successful producer of small cars like the NSU Prinz. In 1967, NSU introduced the Ro 80 a car with rotary-engine, technologies and design well ahead of its time but it became a disaster for the company (for all because of problems with the engines), and resulted into loss of the companies independence. The Neckarsulm plant is now Audi's second "home" in Germany, manufacturing the bigger (in the future MLB) models and home of the quattro GmbH the subsidiary responsible for the high-performance models.

Audi still had a conservative image at this time. The new era after the introduction of the 100 series, and also characterized by the statement (derived from an advertising slogan in 1971) "Vorsprung durch Technik". Under the so called "Piech-era" (Ferdinand Piech, grandson of Ferdinand Porsche was first R&D director, later CEO of AUDI AG until 1993 when he moved to Volkswagen as CEO) Audi was consciously turned into an innovative car manufacturer and the brand was positioned higher.

The technological developments initiated by Piech helped a lot towards the premium status with regard to the innovative brand DNA, which was then followed by the very consciously and planned repositioning of the complete brand identity as a premium brand in the beginning of the 1990's. Until this time Audi's R&D reached a critical point – the company was too small to successfully compete with the big brands Mercedes-Benz and BMW and the brand was also too week against them. Piech's vision was that Audi must develop from one of VW's daughter companies to an independent brand within the VW-group – and this shall mean also greater freedom of action. Nevertheless the expertise-sharing with VW must be forced to reach synergies. Parallel Audi found (or developed) its DNA and positioned itself towards the target customer group with its brand values sporty, progressive, quality: younger, progressive and technique oriented customers[117].

Most important innovations of these times were for example the introduction of the five cylinder engine or the Quattro: the performance car, introduced in 1980, a turbocharged coupé which was also the first German large-scale production vehicle with a permanent all-wheel drive through a centre differential – the solid basis for today's all-wheel drive passenger cars.

The company name was again changed in 1985, this time to AUDI AG. The big change came 1994, where premium became the absolute priority, with the introduction of the A8, using the revolutionary Aluminum Space Frame technology, a real match to the – now – competitors BMW and Mercedes-Benz, but also the complete brand was restructured, beginning with the naming of the models (the Ax naming began) to a new CI and new plans to more than double the production from 300,000 to 700,000.

[117] in: Schmuckstück – Michael Dick, Automotive Agenda 03 Premium lebt!, p. 95-96.

The end of the 80's, beginning of the 90's brought again several technical innovations: fully galvanized bodies, the most aerodynamic volume-built saloon of its time, the extensive use of turbocharged petrol engines, the development of economical direct-injection diesel engines or the aluminum space frame (ASF technology).

Audi is the premium brand with the most mature market positions in China. Audi is present with the joint venture FAW-VW since 1988[118] (beginning with license-assembly of the 100 series) and is now the Nr. 1 premium brand in the country and vis-à-vis China is the biggest sole market for Audi.

In the 2000's Audi was already an equal competitor to BMW and Mercedes-Benz and in 2011 it even overtook Mercedes-Benz regarding worldwide sales numbers.

3.3.2. Innovation

1. Importance of R&D

In case of Audi innovation was the tool to catapult the brand into the premium segment. Volkswagen patriarch Ferdinand Piech had a great role in this process. From his begin at Audi in 1972, as board member for R&D from 1975 and from 1988 to 1993 CEO of Audi, and just as much as later CEO of Volkswagen he put emphasis on technological innovations and established Audi's technological core value, the "Vorsprung". The developments of the 1980's like Quattro, or TDI created the basis for the entry into the premium segment.

No other brand's technological innovations played such a major role on the way to premium, as by Audi. The highlights of these technological innovations are as follows:
- 1980: "Quattro" permanent allroad-drive in passenger cars;
- 1989: "TDI", Turbo Diesel Injection, the first turbodiesel engine with direct injection;
- 1993: "ASF", Aluminum Space Frame, aluminum first used for chasses of a car;
- 1994: 5-Ventile / cylinder technology first used in car engines;
- 2001: The A2 compact car with aluminum chasses has an average consumption of only 3 l / 100 km.
- 2003: Introduction of the DSG automatic gearboxes with electro-hydraulic double-clutch;
- 2004: introduction of the new design language "Single-Frame";
- 2006: "AVS" – Audi Valvelift System
- 2013: "g-tron" – a complex system to reach 100% Co2-neutral driving with a combustion engine.

With the core message "Vorsprung durch Technik", innovation is the absolute priority at Audi. Accordingly, Audi has even as member of the VW-Group an extensive internal R&D capacity: in 2013 Audi employed 9,832 people in the R&D segment

[118] Beginning with license-assembly of the 100 series – source: https://www.audi-mediaservices.com/publish/ms/content/de/public/hintergrundberichte/2014/03/11/audi_in_china/die_geschichte_des.html

(2012: 8,937)[119] – this is 72% of Mercedes-Benz Cars capacity, and the synergy effects with VW are not yet in these numbers.

2. Investing in innovation

As one of the sample brands for the summary chart in Chapter 2, Audi's R&D expenditures were already categorized at *figure 3-8*. Audi is spending even among the premium brands a lot on R&D, in 2013 almost € 4 bn. (more-or-less same amount as Daimler did) or – as set forth in *figure 3-8* – 7.95% of its total revenue. These numbers are remarkable on their own, but with the joint R&D projects with VW it clearly shows that no matter how effective at the present, neither BMW, nor Mercedes-Benz keep up with the R&D capacity of the VW group in the future on their own.

3. Eagerly searching for new segments

As set forth in Chapter 2, The occupation and race for new segments is a characteristics for premium brands and there cannot be another brand for which it is so true as for Audi. After the revival of the brand, but before the expansion to a premium brand, in 1980, Audi had altogether 4 models (the 80, 100, 200 series and the coupe). This was add up with some more other models during the 80's and a big boost in the 90's, for all with the A8 line, the A3, TT, and the S-models. The expansion went on in the next decade and now Audi is having 48 models/derivates (see *figure 3-8*, including S- and RS-models).

4. Cooperation within the automotive industry

As a member of the VW-family, Audi has little cooperation with other OEMs, since it is not needed because of the immense synergy effects with VW (this will be detailed at sub-chapter 3.3.6.).

Tier 1 cooperation is similarity to the other premium brands.

5. Inter-industrial cooperation

In the car-electronics battlefield, Audi and Google joined forces. The cooperation (indeed an alliance) is called "Open Automotive Alliance"[120] and will focus on bringing a successful mobile operating system to in-car entertainment systems, practically the use and further development of Google's Android platform as an operating system in cars**.**[121] Nevertheless Audi is already cooperating with Google within the given Audi systems, such as for example the use of Google Maps and search engine in the Audi navigation systems.

6. Key R&D fields must stay in-house

[119] in: AUDI AG Annual Report 2013, p. 158

[120] Members of the alliance are besides Google and Audi also GM, Honda, Hyundai, and chip-producer Nvidia.

[121] source: *http://online.wsj.com/news/article_email/SB10001424052702304591604579288670734733740-lMyQjAxMTAzMDIwOTEyNDkyWj*; *http://www.theverge.com/2014/1/6/5279116/google-open-automotive-alliance-android-car-announcement*

Regarding this topic, Audi's way of R&D is a very different as of Mercedes and BMW (and similar to Porsche). Since Audi can profit from the synergies with the VW-Group, an own R&D capability was defined as a must for a premium brand, and is accordingly well-established[122], but it does not make sense to double all functions with VW, so some key competences are split.[123]

7. Comparison of KPIs

Differentiation categories		Volume Avg.	Premium Avg.	
Innovation	Expenditure on R&D / total revenue (in %, as of 31/12/2013)	*4,94%*	*8,47%*	*7,95%*
	Number of derivates	*22,67*	*31,33*	*48*
	Number of patent applications in 2013	**37**	*74*	*132*
	Total Number of patent applications as of 30/04/2014	**213**	*334*	*325*

Figure 3-8: Innovation KPIs for Audi

Audis R&D spending and number of patent applications is around the average compared to premium brands – what makes the difference, that beside this spending the huge R&D segment of VW is also at disposal of Audi. Audi has one of the highest number of derivates (a strategic goal in the company's "Route 15" strategy).

3.3.3. Brand building and Sales

1. Transfer of innovation-primacy to the brand

Audi was the one brand that managed to transfer its innovations not only successfully to its brand, but made it the brand DNA. Audi identified at beginning of the 1990's its core characteristics as (s. sub-chapter 3.3.1.) high class, sporty and for all progressive and made innovation its core message: "Vorsprung durch Technik", or the "Truth in Engineering".

This on the other hand goes hand in hand with the responsibility to stay innovative or the most innovative brand. As there were less new features presented first in its models around Audi at the beginning of the 2010's rumors came at once around that Audi has problems and lack innovation[124].

the hypothesis in subchapter 2.4. that motorsport is the best recipe to establish a car brand is very typical for Audi and in this case it could be also translated as the best

[122] in. Dick: Schmuckstück, p. 95
[123] And also quite different model is for example Cadillac, where GM's central R&D headquarters centered in Warren, MI with its international subsidiaries is the common witches kitchen for all GM brands.
[124] in: Rings of Fire; Manager Magazin, 7/2011

recipe to establish a premium brand. Audi used consciously its rally participation and successes to establish the reputation of the permanent all-wheel drive technology “Quattro” in its series models. Audi also used it participation in the Le Mans 24 hours race as a witches kitchen, in 2002 the turbocharged petrol direct injection engines, in 2006 diesel engines or in 2014 laser-headlights – all to boost the reputation of the respective features in series Audi models. Audi is also one of the core participants in the DTM series, nevertheless neither Audi, nor the VW-Group took part at the Formula 1 yet.

2. Brand history and the Premium heritage

If not considering its pre-war record, premium heritage has quite short history at Audi as described in details in the above section, which was the result of the well planned activity to position the brand higher, from a reliable brand of VW to an innovative, progressive independent brand within the VW-Group playing in the same league with other premium brands.

The brand’s reinvented DNA is thus defined by progressivity and technique-orientation. The Design-Innovation-Segment Matrix by Rosenberger and Stürmer define the following key elements to the Audi brand:

	Design	**Innovation**	**Speed** (Segment-specific for automotive)	**Message of the premium brand**
	Functional elegant	Efficiency	Traction	Technical innovation

Figure 3-9: DIS-Matrix for Audi (based on chart of Rosegarten and Strürmer)

3. Sponsoring

Sponsoring at Audi is also defined by the upper-middle class to high-class target customer group. Accordingly the key fields of sponsoring are on the field of event sponsoring, classical or jazz music events, or on the sports sponsoring ski-events[125], sailing (e.g. Audi Sailing Team Germany), but also football (sponsoring of top teams, as Bayern Munich, AC Milan or Real Madrid).

The brand strengthening effects of Hollywood marketing was also realized by Audi, examples therefore are I Robot with Will Smith (2004, Audi present with a concept car) or the Iron Man series (R8).

4. Image transfer from and to other brands and products

The subsidiary Quattro GmbH is responsible for the merchandising of accessories at Audi.

5. Pricing and trims

[125] Skiing is consciously associated to “quattro” in case of Audi, and for this reason a wide campaign was launched in 2013 with the title “the home of Quattro”.

The pricing and trimming concepts as described above are true for Audi as well. The models price range vary according to *figure 3-11* from €16,750 – €127,000, and of course the prices can be highly increased by the extra features.

6. High residual value

Audi is also among the brands with the highest residual value. Besides its premium status, this is also on the one hand strengthened by the common modules used with VW (which enables easier access to a great number of spare parts as the car gets older) on the other hand the relationship with the non-noble family can have effects to the other way. With the same study applied at *figure 3-11* and previously detailed also at Mercedes-Benz, the following Audi models are in the top 3 regarding the calculated residual value for a possible resale in 2017: A6 2.0 TDI and TFSI (Nr. 3 at upper middle class with residual value of 49.5%, resp. nominal value of 18,972.-EUR), A8 3.0 TDI (luxury class, Nr. 3 at residual value with 43% and Nr. 2 at nominal value with 42,465,- EUR), and the Q3 2.0TDI (compact SUV, Nr. 2 at residual value with 56%) – for the actual model-offer definitely less “wins”, then Mercedes-Benz and BMW.

7. Customers and markets

At Audi besides the strong domestic market, two specialties needs to be highlighted: 1: Audi has a weak position in the U.S. premium segment compared to the numerous competitors Mercedes-Benz, BMW, Lexus, Infiniti, Cadillac (with sales of only 158,000 units, half to two/third numbers compared to the competitors)[126] and 2: Audi was in cooperation with VW among the first to be present and build up facilities in the China, which on the other hand means that Audi is with distance the leading premium brand in China which has become its main market in the meantime.

The main markets of Audi were in 2013 the following:

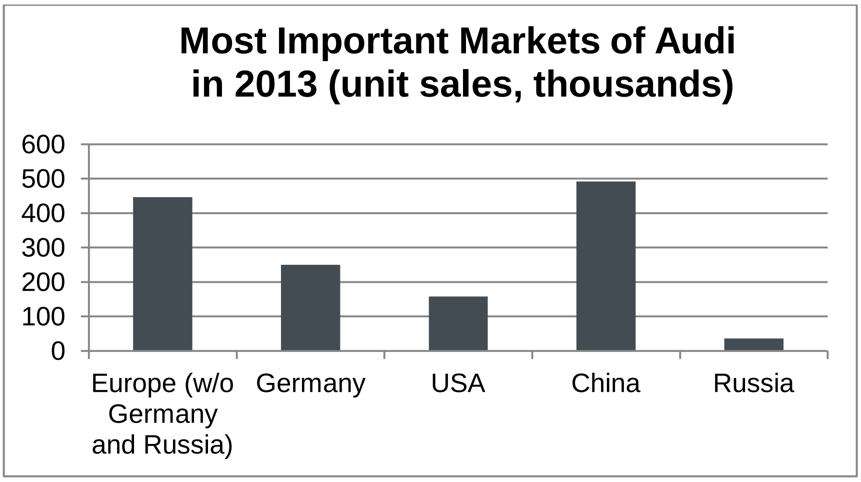

Figure 3-10: Main Sales Regions of Audi in 2013 (author’s chart, based on AUDI AG Press release on deliveries[127])

[126] Audi had a good image and presence in the U.S. market at the beginning of the 80’s which was then ruined by a supposed self-accelerating failure, and Audi is now on the way to regain reputation and be treated as equal to BMW and Mercedes-Benz which has long been reached in Europe and China.

[127] source: *https://www.audi-mediaservices.com/publish/ms/content/en/public/pressemitteilungen/2014/01/09/audi__more_than_1.html*

8. Comparison of KPIs

Differentiation categories		Volume Avg.	Premium Avg.	Audi
Brand Building and Sales	2014 Brand value in $	*9.75 bn.*	*13.8 bn.*	*9 bn.*
	Customer Satisfaction (agg. points in studies)	*780*	*735*	*787*
	Global Sales Growth 2009-2013 (in %)	*24.7%*	*42.8%*	*39.9%*
	Residual value of a typical vehicle (scored points)	*13.5*	*26.5*	*5.5*
	Leasing rate of a typical vehicle (in %of list price / month)	*0.92%*	*1.1%*	*1.11%*

Figure 3-11: Brand Building and Sales KPIs for Audi

The KPI brand value shows that Audi is among the finest premium players not for a long time. The brand value of $9 bn. is only one third of Mercedes-Benz, although Audi sell more vehicles, has a better sales growth (40%) since 2009 and a great customer satisfaction value.

3.3.4. Financial results

1. Price premium

Audi sold in 2013 1.575 million cars – more than ever – with a revenue of € 49.88 billion and EBITDA of € 7.1 billion. EBIT margin was still above 10%. Nevertheless Audi has very strong years of growth behind itself with lots of new production capacities and new models this had an effect of reducing the operating profit which resulted to €5.03 bn., € 335 million less than in 2012.

2. Financial power from own funds

Audi has strong financial positions and a strategy of being able to achieve superior earning power.

3. Comparison of KPIs

Differentiation categories	Volume Avg.	Premium Avg.	Audi

Financial Results				
	Model price range	*€11,370 - €62,9310*	*€29,550 - €395,830*	*€16,750 – €127,000*
	EBIT as of 31/12/2013 (€)	*5.81 bn.*	*4.82 bn.*	*5.32 bn.*
	EBIT margin as of 31/12/2013	*3.6%*	*13.1%*	*10.7%*

Figure 3-12: Financial Results KPIs for Audi

Audi's price range is a bit lower than the average (with Porsche and its €800,000 918 Spyder super sports vehicle), whereby it offers smaller-cheaper models than Porsche, BMW and Mercedes-Benz (Porsche has no sub-compacts, while BMW is selling in this segment under the brand MINI, Mercedes under Smart). Audi has a good EBIT margin of almost 11%, better than the competitors, only Porsche has better margins.

3.3.5. Production

1. Managing complexity
2. Importance of JIS/JIT
3. Flexibility of the production and
4. Emphasis on production in the domestic area.

Audi's production is well integrated within the Volkswagen world. This means the Audi is gaining extra flexibility regarding production by both being able to use plants jointly with other brands of the Volkswagen group as well as being able to profit from Volkswagen toolkit-strategy. This means, that not only diverse Audi models can be built on one single site/assembly line, but also that Audis are built in other production sites within the group (e.g. The Q3 being built in the Martorell plant of SEAT or the Q7 on the same assembly line with the Volkswagen Touareg and the Porsche Chayenne). Many of the components come from other VW-plants and suppliers, but Audi itself has also a huge (partly) component plant in Győr, Hungary delivering almost 2 million engines p.a. for the whole group.

In Europe, Audi has 4 plants: the core plant and company headquarters in Ingolstadt (responsible for both MLB and MQB models), the former NSU plant in Neckarsulm, Germany (an MLB plant, and also home of the Quattro GmbH responsible for the top "RS" derivates), Győr, Hungary (an MQB plant besides the engine, tooling and R&D capacities) and Brussels, Belgium (the A1 family is currently produced here). The MQB plants are flexible and theoretically capable to produce products of other MQB plants[128].

[128] Even before the MQB era, for example in the year 2012, the Győr assembly plant of Audi produced all TT derivates (Coupe, Roadster, S and RS models), the A3 cabriolet and the RS 3 Sportback on the very same assembly line. This is true in an even more complex form for the Bratislava plant where 3-3 models all of which from different brands are currently produced on two assembly lines and this is expected to be extended.

Audi –however still with strong German production capacities – went with VW among the first to China establishing the joint venture FAW-VW plant in Changchun in 1988 and opening the new Foshan plant in 2013. Audi is also present with small assemblies in India (Aurangabad), Indonesia (Jakarta) and Russia (Kaluga) and will open its factory in San Jose Chiapa, Mexico in 2016.

5. Comparison of KPIs

Differentiation categories		**Volume Avg.**	**Premium Avg.**	
Production	Capacity Utilization (2013, in %)	***69.67%***	***n.a.***	***n.a.***
	Flexibility (Nr. of built derivates in the plant)	***3.33***	***9***	***15***
	Production volume/Staff	***36.54***	***16.67***	***22.01***
	domestic production ratio	***36%***	***73%***	***53%***

Figure 3-13: Production KPIs for Audi

Audi's capacity utilization is over the average of the Volkswagen Group's 81%, which means it is clearly above the volume average. The Ingolstadt plant is responsible for the production of several models, and the production effectiveness is (presumably due to the synergies with VW) better, than the premium average. The domestic production ratio is on half way between volume and premium, this is for all because of the extensive capacities of Audi in China (in Changchun more than 400 thousand units produced in 2013).

3.3.6. General Organization and Human Resources

1. Brand independence

Audi is part of the VW family, but creating the independence of the brand within the group was one of the key conditions Audi top management established on the way to become a premium brand – independence as an own company and brand from VW, own and extensive R&D and sales division, but access to and share of knowledge with VW[129].

But Audi is forming a group of its own with the sporty Italian brands Lamborghini and Ducati[130]. These two brands are very different from Audi (Lamborghini is a luxury brand building sports cars, a competitor to Ferrari, while the only 2012 purchased Ducati is a newly acquired motor brand, a competitor to BMW motorcycles), and analogue to Audi's situation, they have independent sales and R&D organization, but

[129] in: Schmuckstück – Michael Dick, Automotive Agenda 03 Premium lebt!, p. 95.
[130] Previously, Seat was also part of the Audi group and then returned as a direct daughter company of Volkswagen

coordinated by the headquarters in Ingolstadt and share the common knowledge within the group[131].

2. Separate and own Organization

Audi has very strong positions within the group and Volkswagen's top management is also often recruited from Bavaria[132]. Accordingly Audi is a full-function entity with 7 board members.

3. Premium brands also use synergies

Synergies from the Volkswagen group is one of Audi's biggest advantage in the market. An important and up-to-date example for the joint R&D activity within the Volkswagen group is the modular building toolkits, a new level of standardisation of which Volkswagen is awaiting a saving in billions while the models of the brands can keep their identities because the standardised parts are overwhelmingly "below the surface". Three such toolkits should suffice for the whole group and the three R&D sovereignty is also split up by those brands who have the most expertise and models that suit the toolkit. The modular longitudinal toolkit (MLB and its newer generation MLB evo) suit for the cars whose engine is mounted longitudinally to the direction of travel (bigger cars, A4-Passat and above), with Audi as responsible for the R&D process. Modular transverse toolkit (MQB), suiting for cars with a transverse engine (smaller car, like the Polo or the Golf) are being developed by Volkswagen and the modular standard toolkit (MSB) will become basis for vehicles whose engine is installed in a longitudinal direction and that feature rear-wheel drive in the base version (sports cars) with Porsche as responsible[133]. Yet, any brand can use the MLB-MQB-MSB technology, if it is offering a suitable and marketable vehicle.

4. Premium brands stays also for premium working environment

Audi is also a popular working place among engineers, as an example it was chosen as one of the best employers among graduates in 2014 (IT: Nr. 1, business: Nr. 2, engineering: Nr. 1 and young professional: Nr. 3)[134].

5. Comparison of KPIs

Differentiation categories		**Volume Avg.**	**Premium Avg.**	
Organization	Brand is a separate company or part of the group company	*n.a.*	*n.a.*	***Separate company***
	Brand organization	*n.a.*	*n.a.*	*7*

[131] For example Lamborghini has significant R&D expertise regarding carbon fibres.
[132] Volkswagen's present CEO Martin Winterkorn, as well as Ferdinand Piech were chairmen of the Audi board before changing to Volkswagen.
[133] Based on Volkswagen Group Management Report 2012 – Synergies and Alliances. Source: *http://annualreport2012.volkswagenag.com/managementreport/value-enhancingfactors/researchanddevelopment/synergiesandalliances.html*
[134] source: *http://www.trendence.com/unternehmen/rankings/germany.html*

	Group synergies	*43.3%*	*34.1%*	*16.2%*
	EBIT / Staff	*19 578 €*	*90 617 €*	*74 115 €*

Figure 3-14: General Organization & HR KPIs for Audi

Audi is not a leading brand within the group, but it is a separate entity, not only managed as a brand but it can live with the advantages as part of a powerful group, Audi volume gives only 16% of the VW-Group total. The EBIT/staff ratio of Audi also corresponds to the premium average.

3.4. MINI

3.4.1 From volume legend to premium - the short history of MINI[135]

Mini was originally an iconic car model, not a brand. Mini, a two-door small car was produced by the British Motor Corporation (BMC) from 1959 until 2000.

The concept of the car was designed by BMC engineer Sir Alec Issigonis with a concept ahead of its time by creating a small car – also affected by the Suez oil crisis of 1956 – that has enough space for the family inside by applying space-saving transverse engine with front-wheel-drive combination layout and small wheels at corners of the car (this also gave the Mini a kind of go kart-like handling).

As written before, Mini did not start as a brand – the model was nevertheless marketed in the beginning under two brands: the Morris Mini Minor and the Austin Seven. in 1961 that Austin Seven was renamed the Austin Mini, and in 1969 Mini became a separate brand. Also sportier versions of the Mini were introduced as Cooper and Cooper "S". Minis were also successful rally cars, winning the Monte Carlo Rally four times from 1964 through to 1967.

During its lifespan the original Mini was produced at various factories by BMC, then British Leyland and finally the Rover Group. In the 1980s and 1990s, several "special editions" of the Mini were rolled out, transforming it from a mass-market vehicle into a fashionable brand. During the1990s the car received a number of updates, such as airbags and fuel injection, nevertheless the car remained relatively unchanged, in relation to its competition, since its original launch. In 1994 BMW acquired the Rover group, though they later sold off much of the group in 2000, BMW kept the Mini and the development on an all-new Mini begun.

BMW launched its new MINI (with all capital letters, differing from the Mini) brand and model. The model developed by BMW was very different car from Issigonis' design classic, but its appearance gave and impression of the classic Mini – However the new model weighted almost twice as much, was longer, broader and used 40 years newer technology.

[135] Chapter based on the following literature: Gottschalk p. 271-272, Simms and Trott p. 228-229, *http://www.telegraph.co.uk/motoring/car-manufacturers/mini/10456893/Mini-a-brief-history.html*

BMW rebuilt also the brand, the association was changed from “cheap” to “cheerful”. MINI’s model range is also being continuously extended, nevertheless all models are still within the same subcompact class.

3.4.2. Innovation

1. Importance of R&D

The original Mini by Sir Alec Issigonis was an innovation on its own – the bold idea of its time by maximizing the cabin and minimizing the chassis, inter alia by introducing a transverse engine or putting the small wheels to the corners of the car. With the introduction of the new MINI under the BMW-era the emphasis was not anymore on the size, but to develop a stylish design icon with go-kart-like driving experience. MINI in this regard did not become an innovation experiment for BMW in the sense of technical features.

By the first new MINI model launched in 2001, although the development process was launched by BMW’s Rover division at the time, with the sale of Rover R&D activities were shifted to the BMW R&D centre in Munich Germany[136]. Ever since, MINI is rather a brand or a subdivision within the BMW Group, than a separate company, research and development is also coordinated by BMW using the group R&D synergies. This also means, that the development of MINI models are integrated in the coordination of other vehicle-projects in BMW’s Product-Creating-Process. This means since the mid 2000’s that similar vehicle projects are in the responsibility of a respective – so called – product-line. All product-lines cover one or two vehicle-segments: MINI variants make up one such segment. The work within the product-lines are interconnected to make use of common resources[137].

2. Investing in innovation

Accordingly, it was not possible during my research from the traceable data to distinguish the exact development costs for MINI within the BMW Group. MINI has access to all BMW developments and BMW also uses MINI for test of innovative technologies, like the BEV “MINI E” In a test fleet of no less than 600 cars or „MINI Connected”, which integrates an internet-based consumer electronics device such as a Smartphone into the MINI[138].

3. Eagerly searching for new segments

If a particular example for the drive for new segments can be named, MINI is a perfect example. In 2001 MINI was introduced as a single stylish retro-vehicle in one single 3-door chassis variant (similar concept, as VW’s introduction of the new Beetle in the 1990’s). Since then MINI introduced several derivates(such as coupe, roadster, convertible, countryman, paceman, etc.) and numerous trims in a way that all of the models are still in the sub-compact (where the core brand BMW is not present) category and the classic 5-door version is being introduced only in 2014.

[136] in: Die Bedeutung des Nationalstaates im Zeitalter der Globalisierung, 2008, p. 16
[137] Source: *http://www.wissen.de/automobilforschung-und-entwicklung-am-beispiel-bmw*
[138] Source: *http://www.bmwgroup.com/publikationen/e/2010/pdf/FIZ_2010_en.pdf*

4. Cooperation within the automotive industry and
5. Inter-industrial cooperation

Cooperation regarding MINI takes place also within the BMW Group development processes.

6. Key R&D fields must stay in-house

As described before “in-house” has a special meaning for MINI, as BMW Group is in charge of R&D processes.

7. Comparison of KPIs

Differentiation categories		Volume Avg.	Premium Avg.	MINI
Innovation	Expenditure on R&D / total revenue (in %, as of 31/12/2013)	*4,94%*	*8,47%*	*n.a.*
	Number of derivates	*22,67*	*31,33*	*10*
	Number of patent applications in 2013	37	*74*	*n.a.*
	Total Number of patent applications as of 30/04/2014	213	*334*	*n.a.*

Figure 3-15: Innovation KPIs for MINI

The only KPI that could be clearly identified is the number of variations. This is only half the volume and third the premium average, but clearly no other player is offering so many derivates of the one single segment.

3.4.3. Brand building and Sales

1. Transfer of innovation-primacy to the brand

The innovation and image-source of MINI is less the innovative high-end technology side, and rather the concept itself and the innovative sales and marketing methods.

BMW reinvented MINI for the 2001 re-launch, by significantly enhancing the value-position, increasing the space and developed the first real premium car in the sub-compact segment.

2. Brand history and the Premium heritage

The premium history of MINI is really short - it began only in 2001 with the introduction of the MINI by BMW. But Mini had even before the BMW times a great almost 50 years history, several rally-wins and with the elderly Mini and several “special edition” models it received a cult status in Europe and – surprisingly – even more in Japan.

BMW kept the marquee Mini from the Rover “package” and reinvented the brand’s DNA. The car and the brand was designed to reach young, trendy and well-off customer groups in the western world. Part of the reinvention was the creation of a new brand identity, with colours and logo, and in order to reach the young, well-off target customer group new innovative and creative sales methods were applied. Beside the classic TV and print media appearances, the MINI marketing staff often applied guerilla-marketing strategies, like putting real size cars on in the billboard on a wall or outing the small MINI on top of a classic U.S. made SUV with the motto “the fun comes on top”[139].

A possible DIS Matrix for MINI can be as follows[140]:

	Design	**Innovation**	**Speed** (Segment-specific for automotive)	**Message of the premium brand**
	fresh and sporty	individuality	go-kart feeling	cool, trendy and very British

Figure 3-16: DIS-Matrix for MINI (own research, based on chart of Rosengarten and Strürmer)

3. Sponsoring

Sponsoring for the brand MINI is not about the size, but about bringing the message through to customers of the cool and stylish car with remarkable sponsoring events. Such are for example the sponsoring of the 2012 London Olympics by delivering ¼ size remote control Minis to deliver various hammers or other staff on the pitch or lifestyle parties within the series “Minimalism”[141].

Sport sponsoring and motorsport is not of such importance in the MINI message, but MINI has some presence in this area as well (e.g. MINI Challenge racing events, or the sponsorship of the smaller Hamburg football club).

4. Image transfer from and to other brands and products

MINI is offering also lifestyle products, real trendy features and apps.

5. Pricing and trims

However MINI is only present in the sub-compact segment, but has a clear premium-pricing strategy, with a price range from about € 15,000 to almost € 40,000. For a car that is the size of a Renault Clio, this is indeed premium pricing, to which several extra features can be ordered as usual in the premium segment.

[139] in, Gottschalk, p. 170
[140] Rosengarten and Stürmer concentrate only on the German core premium brands – the inputs for this particular DIS-Matrix come from the author based on own research.
[141] Source: *http://www.theguardian.com/sport/2012/aug/08/london-mini-sponsor-olympics-2012; http://www.mini.de/minimalism/people/lifeball/*

6. High residual value

MINI is very trendy ever since its reintroduction in 2001 – this has an effect on the used car prices as well. MINI is the champion of residual value in its segment[142].

7. Customers and markets

MINI has also its strong domestic market: MINI is – despite BMW's effect – very British and accordingly almost 20% of all the 305,000 (a plus of 1.2% compared to 2012) cars were sold in the UK in 2013. The other main market is the USA, another good 20% of the manufactured cars go to North America.

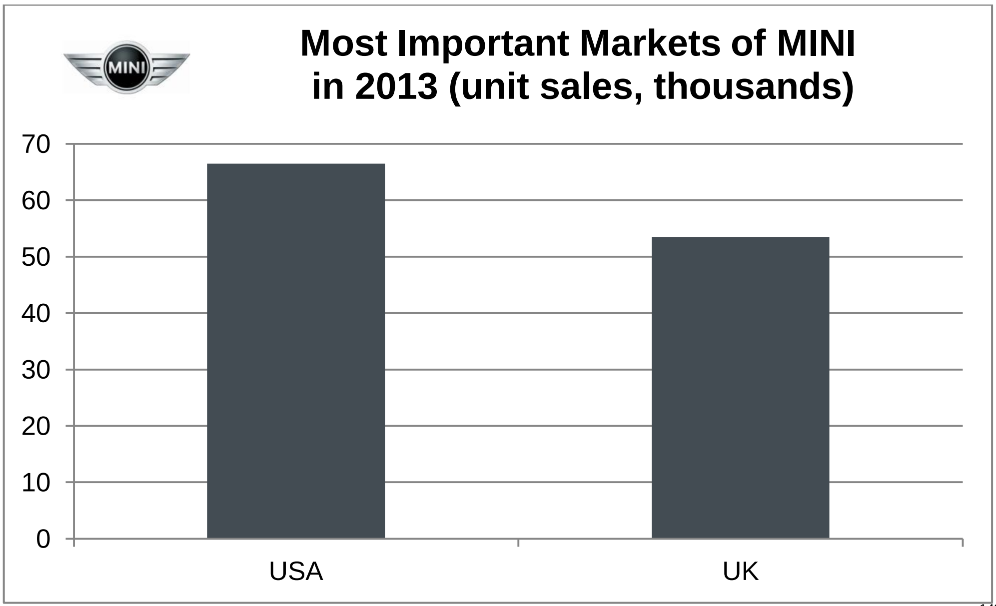

Figure 3-17: Main Sales Regions of Audi in 2013 (author's chart, based on BMW Group Press release on deliveries[143]

8. Comparison of KPIs

Differentiation categories		Volume Avg.	Premium Avg.	
Brand Building and Sales	2014 Brand value in $	*9.75 bn.*	*13.8 bn.*	*n.a.*
	Customer Satisfaction (agg. points in studies)	*780*	*735*	*780*
	Global Sales Growth 2009-2013 (in %)	*24.7%*	*42.8%*	*29.4%*
	Residual value of a typical vehicle (scored points)	*13.5*	*26.5*	*9*

[142] See also at web-pages used for source for residual value KPIs at footnote nr. 64

[143] Source: *http://www.bmwgroup.com/d/0_0_www_bmwgroup_com/investor_relations/ corporate_news/news/2014/vertriebsmeldung_januar_2014.html*

	Leasing rate of a typical vehicle (in %of list price / month)	*0.92%*	*1.1%*	*1.2%*

Figure 3-18: Brand Building & Sales KPIs for MINI

Regarding brand building and sales, quite a few KPIs were accessible also for MINI. The enthusiasm for the brands products are reflected by the high customer satisfaction rate as well as the residual value (there is however a slight contradiction with the relative high leasing rate). Sales growth is only slightly above the volume ratio, which shows, that the segment is probably getting full (more than 300,000 premium cars p.a. for the same sub-compact segment).

3.4.4. Financial results

1. Price premium
2. Financial power from own funds and
3. Comparison of KPIs

Differentiation categories		**Volume Avg.**	**Premium Avg.**	
Financial Results	Model price range[144]	*€11,370 - €62,9310*	*€29,550 - €395,830*	*€17,243 – €37,056*
	EBIT as of 31/12/2013 (€)	*5.81 bn.*	*4.82 bn.*	*n.a.*
	EBIT margin as of 31/12/2013	*3.6%*	*13.1%*	*n.a.*

Figure 3-19: Financial Results KPIs for MINI

Financial data for only the brand MINI was not accessible for the author, so it can only be assumed that the premium prices of MINI models enable high revenues and over-proportional profit despite the production in high labour-cost plants like in the UK and Austria.

3.4.5. Production

1. Managing complexity
2. Importance of JIS/JIT
3. Flexibility of the production and
4. Emphasis on production in the domestic area

MINI's production shows more of the premium characteristics as set forth in Chapter 2, than in case of innovation. MINI models are just as complex as cars of other premium brands – several colors, rims, accessories, trims, etc. Before the

[144] U.K. market, Mini One Hatch vs. Mini Paceman John Cooper Works. Prices converted from GBP with a conversion rate of 1.254 EUR/GBP.

introduction of the new MINI, BMW rethought also the whole production chain: production was kept in the UK (mostly for image reasons), at the same time BMW introduced the production triangle – three plants near each other: Oxford, Swindon and Hams Hall. Five of the MINI models – Hatch, Clubman, Convertible, Coupé and Roadster – are manufactured at the Oxford plant, the triangle also includes the components plant in Swindon as well as the engine plant at Hams Hall, where petrol engines are manufactured for MINI and BMW (diesel engines come from BMW's Steyer Plant in Austria). In Graz (Austria), Magna Steyr Fahrzeugtechnik manufactures the MINI Countryman and, since 2012, the MINI Paceman for the BMW Group[145].

This means, that British domestic production has been (with the exception of the outsourced production to Magna) almost exclusive, but this may change in the future. BMW Group is adding up production from summer 2014 to the Netherlands, to the previously Mitsubishi-plant NedCar now owned by VDL – the production will be on the ten thousands scale. Further is BMW considering to establish a new plant in Mexico, where it may build Minis alongside the BMW 3-series and 1-series[146].

5. Comparison of KPIs

Differentiation categories		Volume Avg.	Premium Avg.	
Production	Capacity Utilization (2013, in %)	*69.67%*	*n.a.*	*n.a.*
	Flexibility (Nr. of built derivates in the plant)	*3.33*	*9*	*9*
	Production volume/Staff	*36.54*	*16.67*	*n.a.*
	domestic production ratio	*36%*	*73%*	*66%*

Figure 3-20: Production KPIs for MINI

Not many KPIs were found for MINI also with regard to production. The main conclusion is from the both identified KPIs that the Oxford plant is a highly flexible facility being able to support all derivates with the exception of the Countyman and the Paceman including the complexity with lots of trims and extra features. Also

[145] Source: *https://www.press.bmwgroup.com/united-kingdom/*

[146] Source: *http://www.handelsblatt.com/unternehmen/industrie/bmw-mini-rollt-ab-sommer-auch-in-holland-vom-band/9496970.html*; *http://www.handelsblatt.com/unternehmen/industrie/expansion-im-dollar-raum-bmw-plant-zweites-werk-in-nordamerika/9887334.html*

interesting that around 1/3 of the MINI production is outsourced to Magna in Graz, Austria.

3.4.6. General Organization and Human Resources

1. Brand independence
2. Separate and own Organization

MINI is not a good example for brand independence and own organization. However it has a distinctive domestic production, lots of central function are incorporated of BMW Group's Munich center.

3. Premium brands also use synergies

The dependence on BMW means of course great synergy potentials with the BMW Group, whereby MINI is only responsible of 15% of the Group sales number.

4. Premium brands stays also for premium working environment

MINI as a brand is a real attractive working place for employees, who want to work at a young and trendy company – a bit like Google among the automotive industry.

5. Comparison of KPIs

Differentiation categories		Volume Avg.	Premium Avg.	
General Organization & HR	Brand is a separate company or part of the group company	*n.a.*	*n.a.*	*not a separate company*
	Brand organization	*n.a.*	*n.a.*	*n.a.*
	Group synergies	*43.3%*	*34.1%*	*15.4%*
	EBIT / Staff	*19 578 €*	*90 617 €*	*n.a.*

Figure 3-21: General Organization & HR KPIs for MINI

Not many KPIs could be identified. As mentioned before, MINI is a special case in the regard that it is more-or-less rather a brand within the BMW world and as such it can profit from all synergy effects of one of the most innovative and successful car producers in the world.

3.5. Summary of the best practice of the three chosen brands

The intention of Chapter 3 was to introduce three successful premium brands, each of them having a different background, different tradition and different strategy and give an overview on the basis of the characteristics and KPIs of Chapter 2, what is common and what is different in their business models.

The following chart is to give the overview of all three brands' characteristics:

Differentiation categories		Volume Avg.	*Premium Avg.*			
Innovation	Expenditure on R&D / total revenue (in %, as of 31/12/2013)	*4,94%*	*8,47%*	*6,55%*	*7,95%*	*n.a.*
	Number of derivates	*22,67*	*31,33*	*40*	*48*	*10*
	Number of patent applications in 2013	37	*74*	*107*	*132*	*n.a.*
	Total Number of patent applications as of 30/04/2014	213	*334*	*562*	*325*	*n.a.*
Brand Building and Sales	2014 Brand value in $	*9.75 bn.*	*13.8 bn.*	*22,5 bn.*	*9 bn.*	*n.a.*
	Customer Satisfaction (agg. points in studies)	*780*	*735*	*715*	*787*	*780*
	Global Sales Growth 2009-2013 (in %)	*24.7%*	*42.8%*	*34%*	*39.9%*	*29.4%*
	Residual value of a typical vehicle	*13.5*	*26.5*	*9*	*5.5*	*9*
	Leasing rate of a typical vehicle (in %of list price / month)	*0.92%*	*1.1%*	*1.1%*	*1.11%*	*1.2%*
Financial Results	Model price range	*€11,370 - €62,930*	*€29,550 - €395,830*	*€24,400 – €233,800*	*€16,750 – €127,000*	*€17,243 – €37,056*
	EBIT as of 31/12/2013 (€)	*5.81 bn.*	*4.82 bn.*	*4.0 bn.*	*5.32 bn.*	*n.a.*
	EBIT margin as of 31/12/2013	*3.6%*	*13.1%*	*6.2%*	*10.7%*	*n.a.*
Production	Capacity Utilization (2013, in %)	*69.67%*	*n.a.*	*84%*	*n.a.*	*n.a.*
	Flexibility (Nr. of built derivates in the plant)	*3.33*	*9*	*7*	*15*	*9*
	Production volume/Staff	*36.54*	*16.67*	*16.2*	*22.01*	*n.a.*
	domestic production ratio	*36%*	*73%*	*68%*	*53%*	*66%*

General Organization & HR	Brand is a separate company or part of the group company	**Not a separate company**	***n.a.***	***not a separate company***	***Separate company***	***not a separate company***
	Brand oganisation	**18**	***n.a.***	8 (responsible for brand and group)	***7***	***n.a.***
	Group synergies	**n.a.**	**43.3%**	***93.6%***	***16.2%***	***15.4%***
	EBIT / Staff	**22 614 €**	**19 578 €**	***41,282 €***	***74 115 €***	***n.a.***

Figure 3-22: Summary chart for Chapter 3

Three successful but fairly different premium brands have been examined in this chapter. Mercedes-Benz is a leading brand with great luxury and premium tradition of an extensive automotive group, Audi – having also a hundred years of history but still a fairly new player of the premium segment – is an important but relatively moderate part of one of the biggest automotive players in the world, while MINI has less and less to do with the basic Idea of Sir Issigonnis and is rather a sub-compact BMW with a strong and individual DNA made in Britain. These three different very characteristics show that there are multiple ways to be a successful premium brand.

The main findings of the one topics are as follows:

1. Innovation

Mercedes-Benz and Audi are similar in their capability of innovation, but Audi can spare costs or concentrate on some particular R&D field with Volkswagen's R&D power and economies of scale behind. Mercedes-Benz has only Smart to share the developed technology, and until even so it could keep up with the competitors, but as time change and the importance and costs of R&D rise, it must seek cooperation with Tier 1s, as well as other OEMs to be able to keep up with the competitors. MINI itself is making a living on the one hand of its design (which is a key development field in case of the British brand), on the other hand of BMW's "treasure chest".

R&D expenditure shows that both Mercedes-Benz and Audi are spending around (a bit below the average premium level on R&D – but both definitely more than volume players, but in proportion Audi spends more. Accordingly Audi has some more derivates, some more pending patents but in total less patent applications than Mercedes-Benz. If we add Volkswagen's group development capacity to these numbers, Audi has in the future clearly an easier way than Mercedes-Benz most probably will. The accessible data shows that MINI has almost a quarter of derivates than both other brands, but this only for one segment – an exceptional proportional variety of models – a big question where are the (or whether there are any) future growth perspectives for MINI (also taken account that BMW has recently founded a sub-brand for its full-hybrid/BEV models, the BMW i, which even more limits MINI's future growth concepts).

2. Brand building and sales

All the three are very strong brands, for all Mercedes-Benz with a brand value more than twice the volume average, but their own customers' satisfaction is not necessarily better than of volume brands. Audi's shorter premium history is also well indicated in its brand value which is rather comparable to the volume average than the premium.

Regarding customer satisfaction there is no significant difference between the three brands (as this is true also for the other examined volume and premium brands).

Sales growth is comparable at the three examined premium brands. The biggest growth rate was at Audi, Mercedes-Benz has had somewhat lower growth (as Mercedes-Benz has struggled somewhat with respect to sales against Audi and BMW) but still over 30% - according to sales results in 1st half of 2014 Mercedes-Benz would have an better position if 2014 was also considered. MINI's sales are slightly below 30%, an indication that MINI stocked up the segment in which it is present. The volume brands' growth of 24.7% is clearly below the data from the three analyzed premium brands.

The values of used Audis, Mercedes-Benzes and MINIs are also kept way better than respective volume models and customers are eager to buy them. The leasing rates however do not mirror this residual superiority.

3. Financial results

All three brands have strong financial foundations and are really profitable for their respective shareholders (this is presumed also for MINI, even if I did not manage to find corresponding data), indeed way more profitable than volume brands.

From the three brands, the price range of MINI seems to be relative narrow – of course because of the also narrow model range. Audi and Mercedes-Benz prices are about the premium average.

As regarding EBIT margin, Audi's is making proportionally 1.5 times as much profit as Mercedes-Benz – this has probably a lot to do with the synergy effects from the Volkswagen Group and indicates that Mercedes-Benz needs allies to save costs and retain premium profit level (however the profit rate of Mercedes-Benz is still double of the volume average).

4. Production

Regarding production, all three brands have a lot of derivates (in case of MINI proportionally – since it is present only in the subcompact class) and provide and endless list of extra features and so possible combinations for the order management and production. These three brands can all cope successfully with this complexity, however this also shows that they need more staff than volume brands to do so. All the three brands (still) have strong domestic production capacities (however by Audi only each second model, by Mercedes-Benz and MINI two out of three come from the homeland production facilities), but as this game goes even more global, the trend is that the production facilities will also balance corresponding to main markets.

5. General Organization & HR

The organization of the three brands is very different. The brand Mercedes-Benz is giving more than 90% of the Daimler car production, and the concept of the Smart brand (mini cars) is also quite different. Several members of the board of management of Daimler are having double functions: Group function and responsibilities for Mercedes-Benz Cars – this shows that the division Mercedes-Benz Cars (and thus the brand Mercedes-Benz) is indeed the way strongest foundation of the Daimler group providing all the necessary resources to build the brand but also needing allies (e.g. Renault) to achieve synergies and save costs – it will turn out in the close future whether Mercedes-Benz can succeed with this strategy and keep the brands core DNA. Audi is a part – the most valuable – of the Volkswagen Group. Audi does not need other allies within the OEMs, it has different challenges, use as much synergies from the VW world as possible but keep its independence in terms of own R&D and sales-brand building and avoid the image "overpriced rebadged VW" in order to remain an equal competitor to the other premium brands or even to achieve its utmost goal: to become the Nr. 1. MINI has compared to Mercedes-Benz, but even compared to Audi few independence: MINI is considered rather as just a brand than an automotive subsidiary of BMW. Diverse functions (e.g. key R&D functions) regarding MINI are in the responsibility of BMW management and yet BMW succeeded to re-establish a brand with remote-control from Munich and find and evolve the brand's core DNA so that it is "very British", and could successfully reach young, well-off customers. But the great idea behind MINI (a retro design with up-to-date technology of the old Mini) shows also the future (or even already present) challenges of this brand: on the one hand where is the frontier of the expansion of the MINI derivates (or would be accepted by the customers and would not hurt BMW's product portfolio if other bigger models would be brought to market) on the other hand the hard design work to keep the retro design trendy and "sexy" through generations of the model. Until now BMW managed this challenge also successfully.

The essence from the success of the three examined brands is that there is no golden rule, but different approaches towards premium power with specific similarities regarding the nature of premium business.

Chapter 4: Summary and quick outlook in the future of the segment

This chapter is meant to give a short abstract to the findings of this Master's Thesis but a summary cannot be complete without giving an estimation about the future, whether the findings can be – in the opinion of the author – sustainable in the future of this business and what can be the future challenges for the industry.

The purpose of this Master's Thesis was to identify the key areas of an OEM-s strategy, where a different approach is needed, if compared to a volume brand or a budget brand and to observe this on particular examples (four case studies) and also spot the different ways of premium strategies.

4.1. The definition of a premium automotive brand

The aim of Chapter 1 was to establish the basis of the present Master's Thesis by giving a definition of a premium automotive brand based on different approaches and definitions already in the common sense and the literature.

From the many possible definition and characteristics I chose to identify the following features as primary characteristics of a premium brand:
1. brand heritage with a high symbolic value;
2. high degree of innovation and investing over proportionally in innovation;
3. quality image;
4. high complexity production in greater lots; and
5. premium price, which must be reinvested to keep the above mentioned premium features.

4.2. What makes all the difference? The premium strategy examined at three successful and an unsuccessful examples

In Chapter 2 the key business fields were identified on which the case studies of four brands were established. The identified key business fields were: innovation, brand building & sales, financial results, production and general organization & HR. Also, some KPIs were introduced in order to be able to verify the assumptions with facts where possible.

In Chapter 3 three successful premium brands was examined. In the chapter the key business fields and also the KPIs defined in Chapter 2 were examined. The results showed that there are multiple ways (for all regarding the organization of a premium brand) to be successful in the premium automotive business, but all successful brands have also several characteristics in common. Shortly the examination of the four brands Mercedes-Benz, Audi and MINI led to the following consequences:

- **Innovation is a must** (MINI cars also receive the newest technologies from BMW but own innovation is rather on the design side in case of MINI), just as **finding and consequently building the DNA of the brand**.

- This must be brought to a **complex production with all derivates, trims building to order** of the customers.
- Premium brands also need the **organization that enables them the necessary innovations and does not choke the independence of the brand** within the group (keeping the DNA of the brand) – beside R&D, the sales and brand-building activities are important to be kept relatively independent from the group headquarters.
- These circumstances give the foundation of an innovative brand (design as well as applied technologies) with the tradition/DNA that enables customers to identify themselves with the brand. **These foundations lead to customer demand of the products of the brand**.
- With customer demand given, the **premium price can be applied** (in this regard premium players try to define their prices around the level of the competitors), which **enables the premium profit**, the essence of the premium business.

Regarding the different practices the way of organization and level of independence was the biggest identified difference between the three successful premium brands. It turned out that a premium brand can be successful as a leading brand of an automotive group with several joint functions of the brand and of the group on top management level and where most resources are dedicated to the benefit of the premium brand (Mercedes-Benz). Another way of success is one – not leading – brand within a group, whereby wide independence on the fields of R&D and sales/brand building is provided and parallel the extensive synergy effects are used (Audi). A third observed way was rather of recreating a brand, providing it with revitalized brand DNA and great design and from the group resources providing with up-to-date innovative technologies (MINI).

4.3. What can the future bring?

Analyzing the possible future scenarios of the premium automotive market is rather a subject of thesis of its own, but for the big picture I chose to end the present Master's Thesis with a very rough vision of my personal assumptions regarding the close future.

The future of the premium automotive segment seems to be bright but not without difficulties and risks.

On one hand the position of the premium car brands on their mature markets like the TRIAD (Europe – US – Japan) is likely to stay stable, while the BRIC markets (and for all China) have real market demand for – not only automotive – premium products. China is already the biggest sole country market for Audi (see figure 3-10) and McKinsey&Company sees in a study of 2012 China by 2020 as the way biggest market for premium automotive products and Russia a larger market than France[147] (see figure 5-1). This makes the leading automotive groups a must to stay or get involved to the premium business if they want their not only market but also profit share from the BRIC and other emerging markets.

[147] Upward Mobility: The Future of China's Premium Car Market, McKinsey&Company, 2012, p. 4

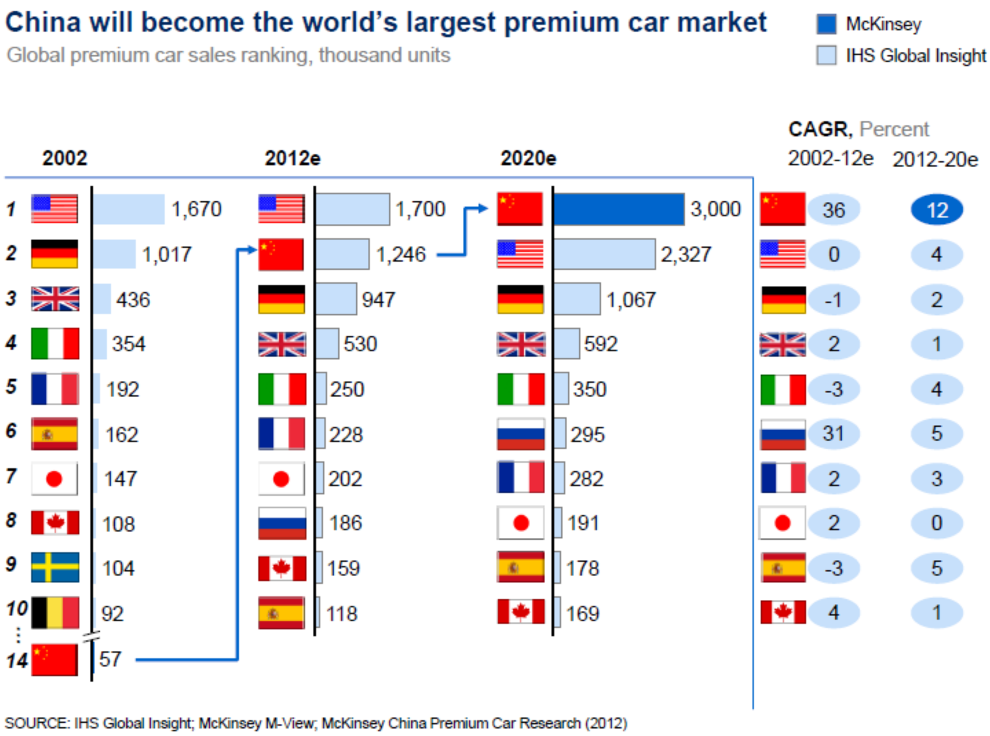

Figure 5-1: China will become the world's largest premium car market (source: McKinsey&Company)

But the future of the premium automotive business is not without challenges. A great challenge is urbanization and the ongoing change in customer habits: "With more than 60 percent of the world population expected to live in urban cities by 2025, urbanization as a trend will have diverging impacts and influences on future personal lives and mobility. Rapid expansion of city borders, driven by increase in population and infrastructure development, would force city borders to expand outward and engulf the surrounding daughter cities to form mega cities, each with a population of more than 10 million. By 2023, there will be 30 mega cities globally, with 55 percent in developing economies of India, China, Russia and Latin America. The mega cities from emerging economies will witness a Compound Annual Growth Rate (CAGR) of 4.4 percent in GDP (PPP) from 2009 to 2025, as compared to a CAGR of 1.63 percent for the same period in the mega cities from developed economies"[148].

The urbanization is likely to change customer habits: predictable a major part of the future buying power will live in crowded, polluted cities. Providing mobility under these circumstances is hard. In these cities a different kind of mobility shall be provided, than for the people in for e.g. rural Europe. Mobility will mean for all public transportation, scooters, electric vehicles also of non-combustion propulsion and full hybrid cars, maybe in very small portion also fuel cell powered cars, foreseeing with more and more connected, online and/or autonomous functions. It is probably, that outside this megacity areas, the demand for bigger, but also efficient cars and commercial vehicles will remain. Another already ongoing change in the urban areas is the decline of demand for the possession of a car – premium brands must be ready

[148] in: Urbanization Trends in 2020: Mega Cities and Smart Cities Built on a Vision of Sustainability, source: *www.frost.com/prod/servlet/cpo/213428721.pdf*

to provide services (like car sharing[149]) or re-invent their brands (e.g. for scooters) if they want to be present on a large scale on the urban markets of the future.

Summarized the premium (automotive) business will definitely have a future, but the question is which of today's (or future) brands will be more fit and prepared for the possible changes.

[149] Mercedes-Benz and BMW already have with their subsidiaries „Car2go" and „DriveNow" extensive car sharing facilities in multiple metropolitan areas

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