Rediscovering Profitability and Value in the Auto Sector

Frits K. Pil

Discussion by
Chad Syverson
Univ. of Chicago

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Biggest Problem with Push Strategies: Overproduction

Overproduction imposes short- and long-run profit losses:

- Creates additional inventory costs
  - Dealers angry too
- Increases use of incentives (i.e., lowers vehicle price)
- Encourages dumping into rental fleets
  - Lowers future sales prices by flooding market with used vehicles
  - Presents “plain face” to consumers

Very efficient BTO operation would avoid overproduction problems

- But implementing is very costly for a complex production chain

Better Forecasts Would Help—Even without BTO

Many problems could seemingly be solved if forecasts were more accurate, even if no shift to BTO is made

How? Aren't firms already making best possible forecasts?

Internal markets

- Let interested parties trade bets on success of proposed models
  - E.g., mktg., production, upper mgt., dealers, suppliers, etc.

- Excellent way to aggregate diffuse information

- Pilot at large "big-box" retailer shows promise for predicting firm financials, sales of particular products, etc.

- Can these be run without giving too much proprietary info away?

Moving Toward BTO—Too Many Dealers?

Dealers provide useful services, but can be a drag on pure BTO efficiency

- If you’re going to order a car, why not go straight to the source?
- Internet and e-commerce infrastructure facilitate direct orders to producers
  - Ex: purchases of travel services often bypass travel agents

Franchise laws protect low-quality dealers

Despite this protection, there is evidence that e-commerce has already started forcing some dealers out

Moving Toward BTO—Too Many Dealers? (cont.)

	Dealer counts by employment size category				
Year	10-19	20-49	50-99	100-249	250+
1994	4,142	9,017	4,853	1,601	78
1999	3,611	8,616	5,437	2,083	135
2003	3,394	8,237	5,768	2,532	231
Change 1994-2003	–748 (–18%)	–780 (–9%)	+915 (+19%)	+931 (+58%)	+153 (+196%)

Decline in smaller dealerships and growth in larger ones is tied to local growth in consumer e-commerce use

- Less effective intermediaries are leaving market
- Internet search and larger dealers might also partially solve customization problem (larger real and virtual inventories)

Moving Toward BTO—How Will Consumers' Tastes for Variety Change?

Maybe BTO doesn't require as much customization as we might think

- Ex: For many vehicles, 0.1% of model variants account for 50% of sales

But this is an "equilibrium outcome"

Consumers don't consume many varieties because doing so is costly

- Instead willing to fit square peg in round hole

But if BTO becomes the modus operandi, variety of orders could increase substantially

Moving Toward BTO—Is Labor Flexible Enough?

Purely from production perspective, automakers have little incentive to idle plants

In this industry, labor is like capital—pay for it whether used or not

- Capacity utilization decision is too discrete: basically on/off at shift level

Considerable effort and time might be required to change contractual arrangements to build in flexibility

- Vertical disintegration as a path to capacity flexibility throughout production chain?