STA Presentation

Shifting Gears – How to ride the wave of change in the automotive industry?

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Riding the wave of change in the automotive industry….

Introduction

Carlos Ghosn said at the opening of last year's New York International Auto Show:

"I expect the global auto industry to see more changes in the next five years than it has in the last twenty".

He continued by saying:

"Because for those open to new ideas and new ways of doing things, the opportunities for our industry to grow and better serve society's needs has never been greater."

Image source: Renault-Nissan

The automotive industry is facing the biggest change in history due to several trends caused by legislation, society, technological developments

Key automotive trends 2017ff

Technology Trends

1 Electrification

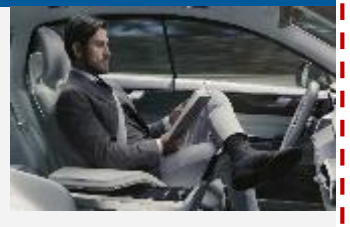
- Increased penetration of electrified powertrains
- Electrical power becomes scarcer and tightly managed
- Range vs. functions trade-off
- New styling freedom in purpose-built xEV

Connectivity

- Increased connectivity in vehicles
- Increased data exchange (car2car, car2infrastr., car2x)
- Increased digital services in the automotive eco system

2 Autonomous Driving

- Increasing levels of autonomous driving from hands-off to mind-off
- Based on superior hardware for sensors and artificial intelligence
- Enabled through new software for object recognition, trajectory planning and actuation



Business Changes

Mobility as a service

- Decreasing attractiveness of traditional car ownership model
- Lease- or opportunity-based usage models
- Multi-modal transport solutions
- Cross-OEM and cross-modal solutions
- Digitals as new entrants

Changing Industry

- New vehicles, new markets
- New players and business models
- Changed volume structure (e.g. less cars due to Robotaxis)
- Changed price structure (e.g. decreasing margins due to xEV)

3 Digitalization

- Internet of Things / Industry 4.0
- Agile strategy and business processes
- End consumer driven

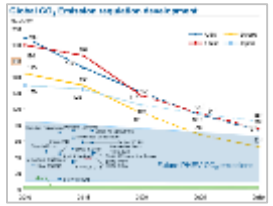
Source: Strategy Engineers, pictures are public source

Riding the wave of change in the automotive industry

- **Electrification**
- Autonomous Driving
- Digitalization

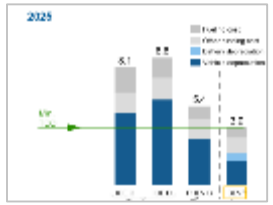
Four major drivers will lead to increasing xEV market shares beyond 2020 – CO_2 regulation, TCO, electrical range and increasing charging infrastructure

Drivers for increasing xEV market share



1 Legislation and stricter CO_2 targets

The increasing pressure to reduce pollutant emissions and CO_2 emissions and introduction of real driving emissions creates the need for pure EVs

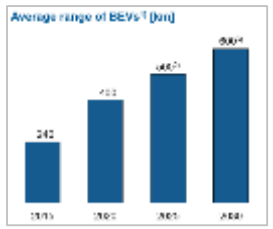


2 Competitive total-cost-of-ownership (TCO)

When the total cost of ownership for EVs reaches break even, electric vehicles become increasingly attractive for a larger number of costumers

3 Increasing electric range

Increasing pure electric ranges will soon meet customer demand



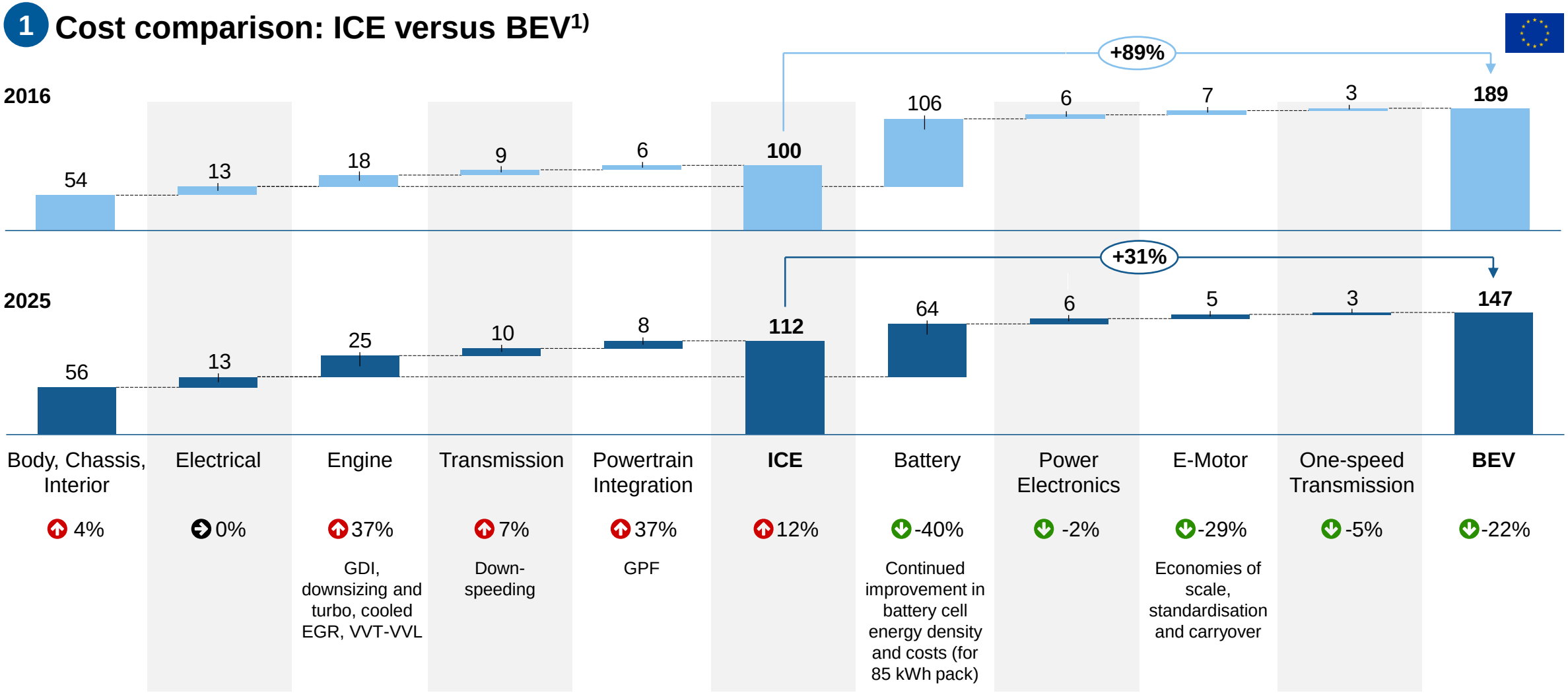
4 Increasing availability of charging infrastructure

Increasing charging options to secure customers' demand

Source: Strategy Engineers // TCO: total cost of ownership

BEVs will gain a solid material cost advantage over ICEs soon – Point of cost parity depends on battery cost decrease

1 Cost comparison: ICE versus BEV[1)]

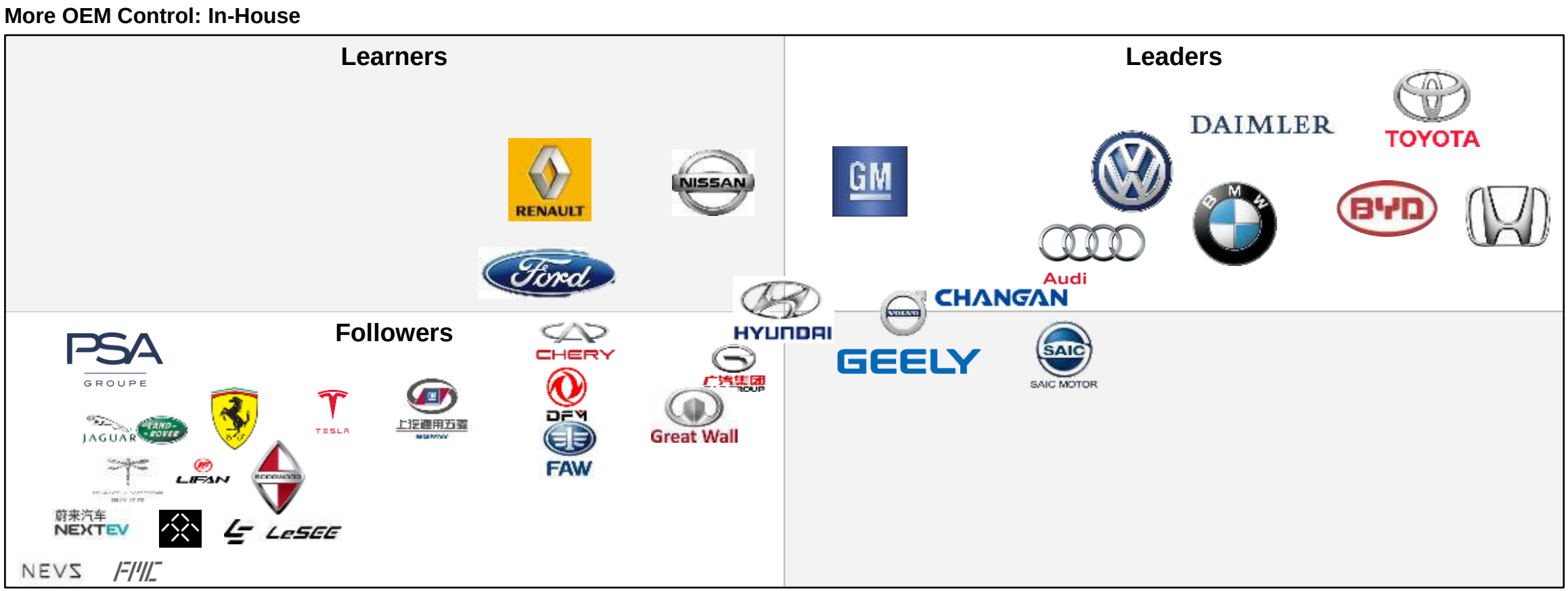


Source: USABC, SAE, IKA, Strategy Engineers analysis and estimates // [1)] Europe C segment vehicle; 2016, Costs module incl. Battery management system: 120 €/kWh – 2016, 80 €/kWh - 2025

OEMs employ different strategies when it comes to engineering and manufacturing of xEV systems

1 OEM engineering and manufacturing strategies

ILLUSTRATIVE



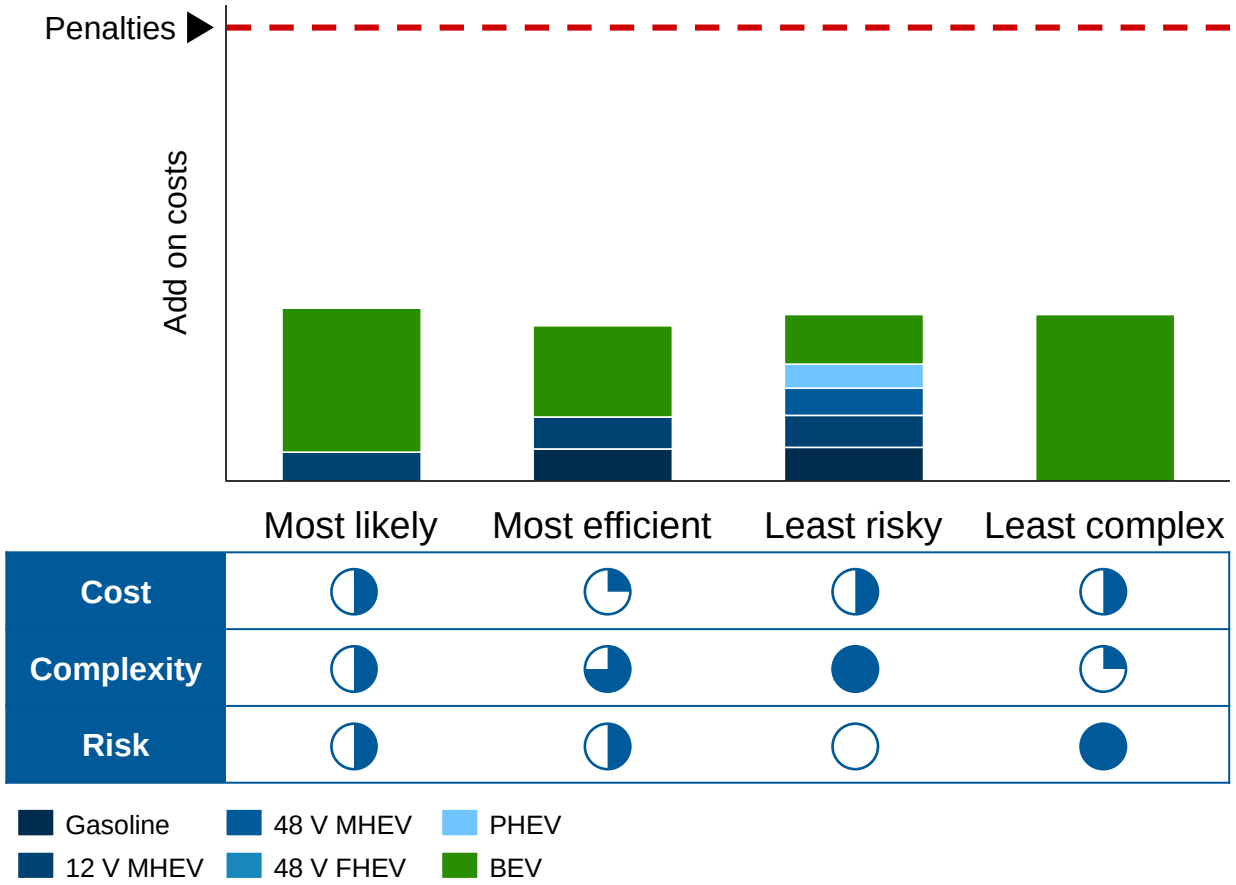
Source: Strategy Engineers

From a strategic and financial viewpoint, exposure to the risk of penalty costs is not feasible – xEV vehicles must be pushed onto the market

1 CO_2 reduction strategies simulation

CLIENT EXAMPLE

Simulated scenarios



Comments

- Penalty → worst option: **always** much more expensive
- **BEVs necessary** to achieve CO_2 fleet targets 2021/2025
- Betting only on **BEVs** is too risky: the required market share needs **high subsidies**
- **Hybrid technology** is a valuable complementary solution
- Further **improve ICE technologies** for Gasoline to reduce required share of xEVs
- Keep the **portfolio mix complexity low** to avoid an overload for the R&D effort and reduce the risk of project delays

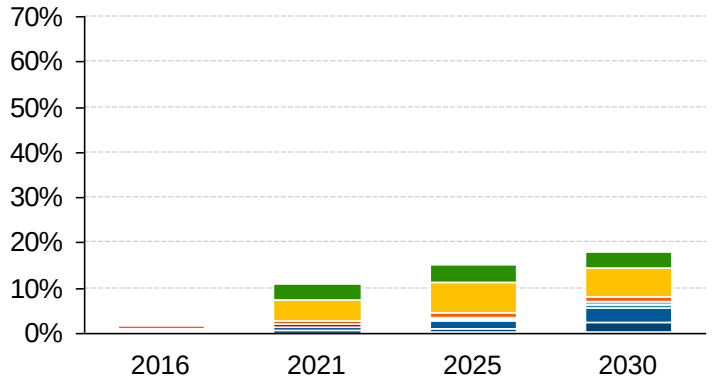
Source: Strategy Engineers, AVL

xEV customer demand (pull) is strongly dependent on OEM pricing decisions

1 xEV customer demand (pull)

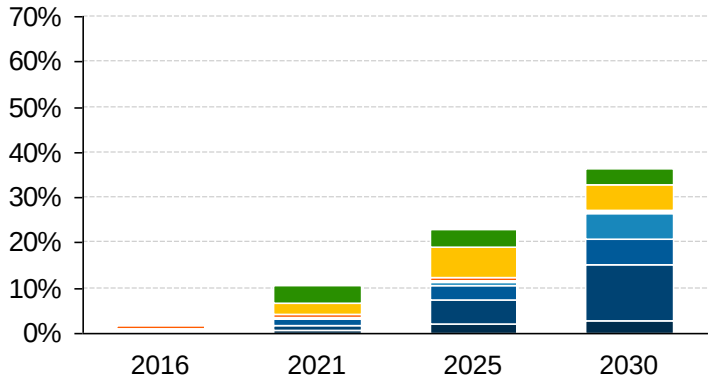
Conservative scenario

OEM markup on			
Battery pack	50%	Other components	50%



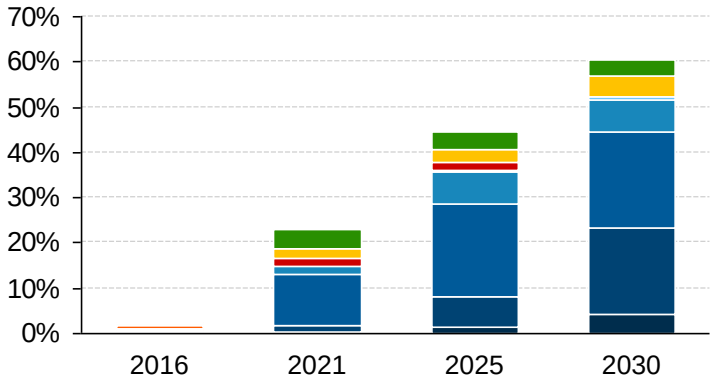
Mild scenario

OEM markup on			
Battery pack	25%	Other components	50%



Aggressive scenario

OEM markup on			
Battery pack	0%	Other components	50%



Figures indicative

OEM decisions in term of gross margin are crucial for the diffusion of xEVs

- **Aggressive scenario** to be considered only if fast BEV diffusion is required by CO_2 emission regulations (battery pack R&D and production costs need to be covered by alternative founding)
- **Conservative scenario** is to be considered only if government will strongly support BEV sales by introducing high economic incentives

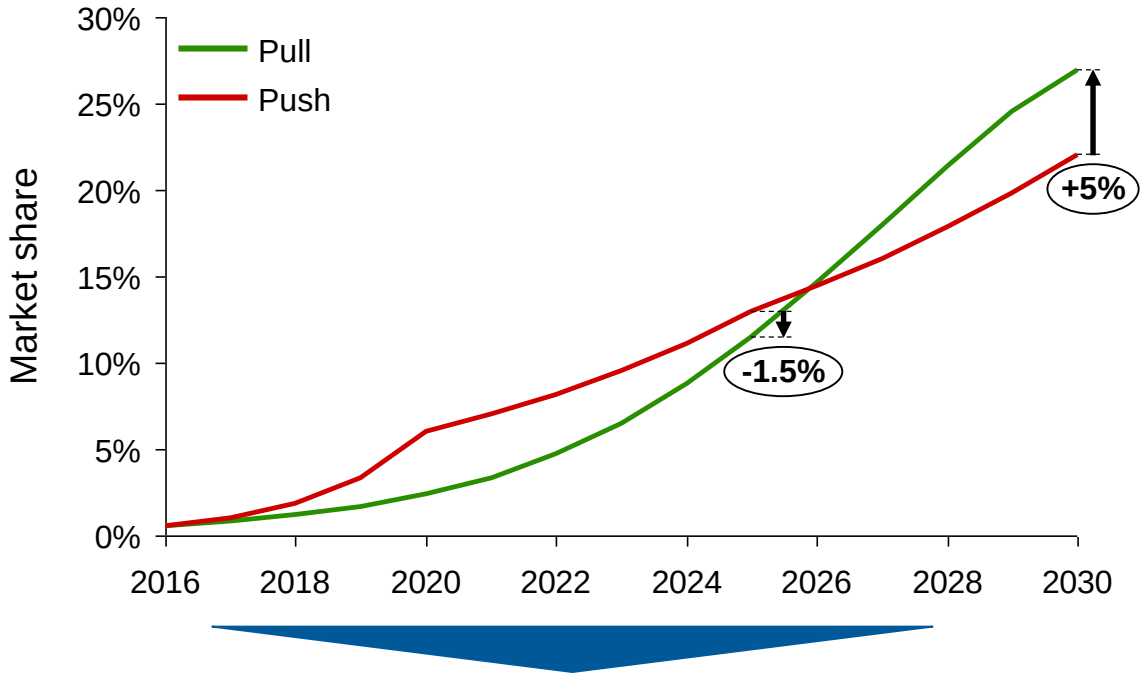
A BEV B BEV C BEV D BEV E/F BEV A PHEV B PHEV C PHEV D PHEV E/F PHEV

Source: AVL, Strategy Engineers

BEV pull is aligned with push forecasts, whilst PHEV diffusion is expected to slow down by 2030

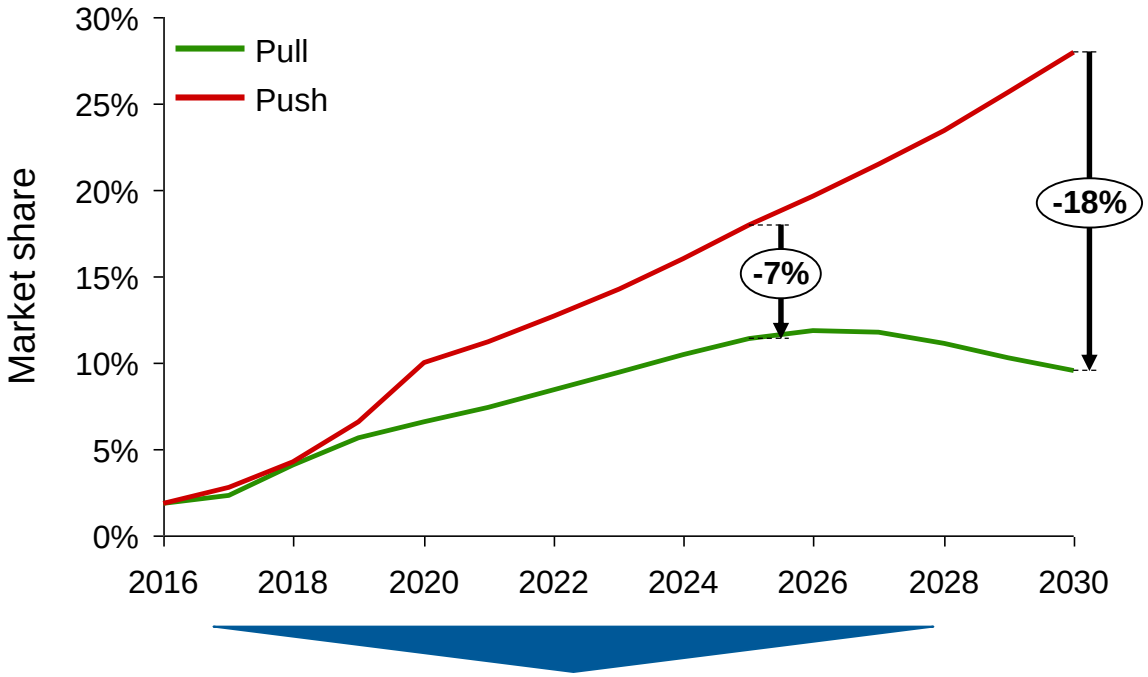
1 Push vs. pull model (mild scenario)

BEVs



Pull demand of BEVs is aligned with market push to comply with CO_2 emission regulations

PHEVs



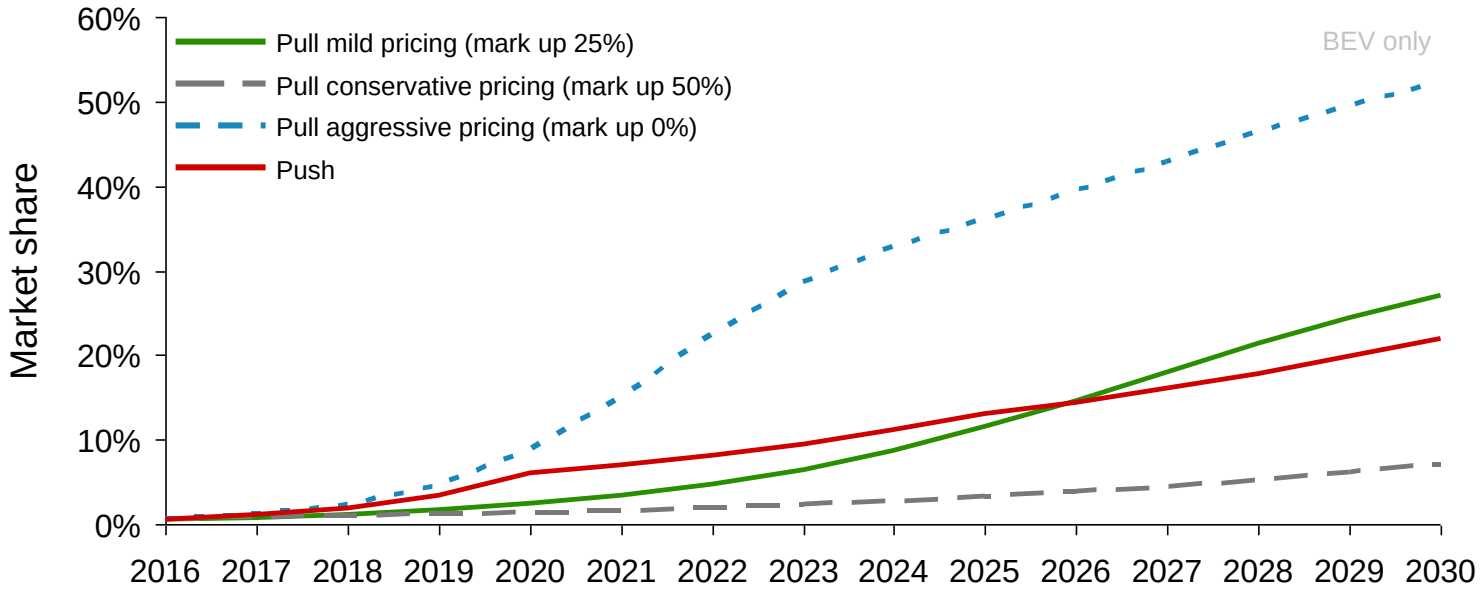
PHEV technology is too expensive for penetrating the market as much as needed by the CO_2 emission requirements

Source: AVL, Strategy Engineers

According to different pricing strategies, customer demand presents high variation

1 Push vs. pull model

Pull effect according to different pricing strategies (BEV)



Pricing assumptions			
Mark-up on components cost (excl. battery pack) for all scenarios			50%
Mark-up on battery pack cost	0% (aggressive)	25% (mild)	50% (conservative)

Comments

- According to different pricing strategies, customer willingness to buy (pull) can be strongly influenced
- Pricing strategies must take regional and local subsidies into account, to keep the pull demand as close as possible to the required push
- In case the pricing strategy is too aggressive, the financial stability of the automotive industry can be threatened
- A too conservative pricing strategy can lead to a low diffusion of BEVs, leading to the payment of penalties

A winning pricing strategy must be defined

Source: AVL, Strategy Engineers

Pure electric vehicle sales are expected to take off once attractive products become available – aggressive pricing and discounts will lower margins

1 Summary Electrification

- **Legislation** in Europe (but also China and US) will demand **fleet electrification** from 2020 onwards
- Key for OEMs will be the **most cost-effective powertrain mix** in balance with **customer demand**
- **Prerequisite for customer demand** is an attractive product offer, most importantly a **reasonable electric range** and **competitive cost** compared to conventional ICEs, i.e. a price-competitive volume EV with an electric range above 400km
- **Hybrid powertrains** are a **bridging technology** to facilitate the transition from conventional powertrains to EVs; hybrids lack a superior value proposition over EVs to justify a long-term market success
- Hence, **conventional powertrain improvements**, the introduction of **MHEV in small segments** and the launch of **multiple BEV vehicles** are the most likely option
- Electric powertrains will become **needed** as a consequence, with radical changes for OEM **engineering processes, value chains and manufacturing footprint**
- OEMs need think about **pricing strategies to fulfil needed EV quotas** – **Aggressive pricing and discounts** are likely required to achieve targets and avoid penalties

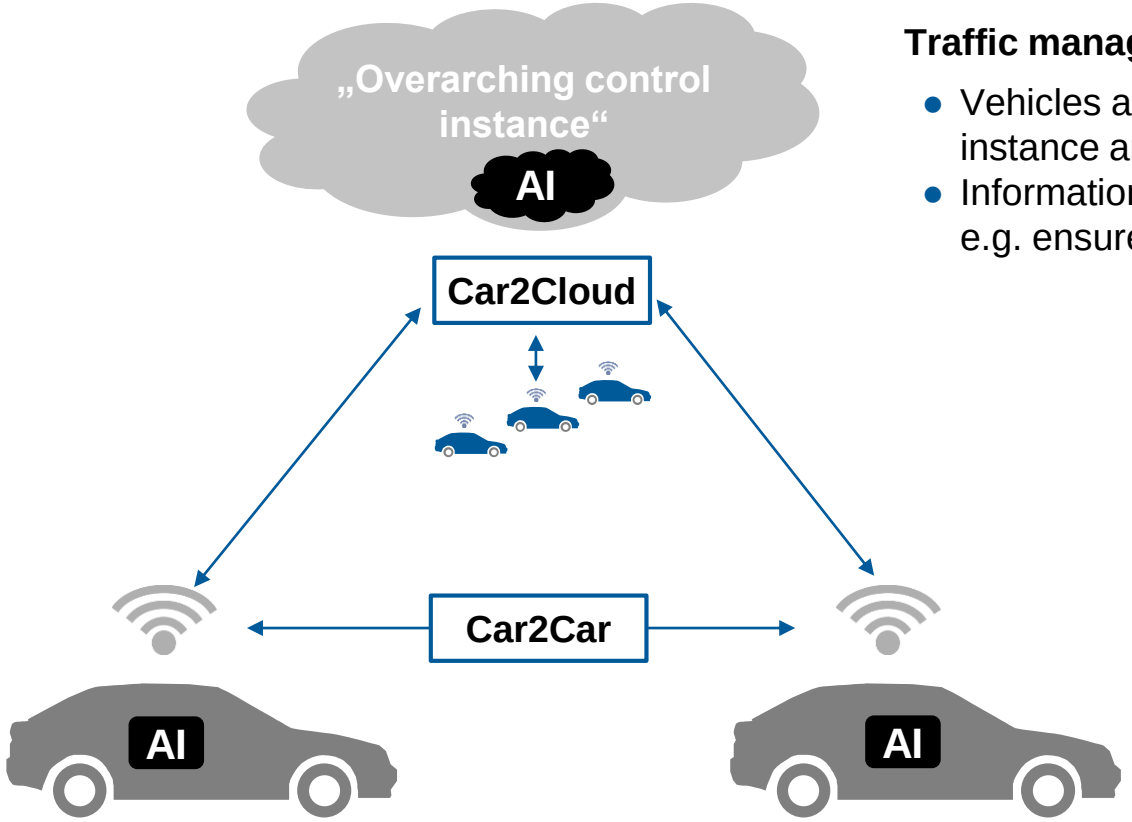
Source: AVL, Strategy Engineers

Riding the wave of change in the automotive industry

- Electrification
- **Autonomous Driving**
- Digitalization

Stand-alone „driving robots“ cannot guarantee full safety and efficiency – they have to be integrated into a comprehensive traffic network system

2 Connectivity as condition for autonomous driving



Traffic management - Car2Cloud connection

- Vehicles are permanently communicating with overarching control instance and act as actuator and sensor at the same time
- Information is selectively distributed across traffic system in order to e.g. ensure homogeneous free-flow traffic

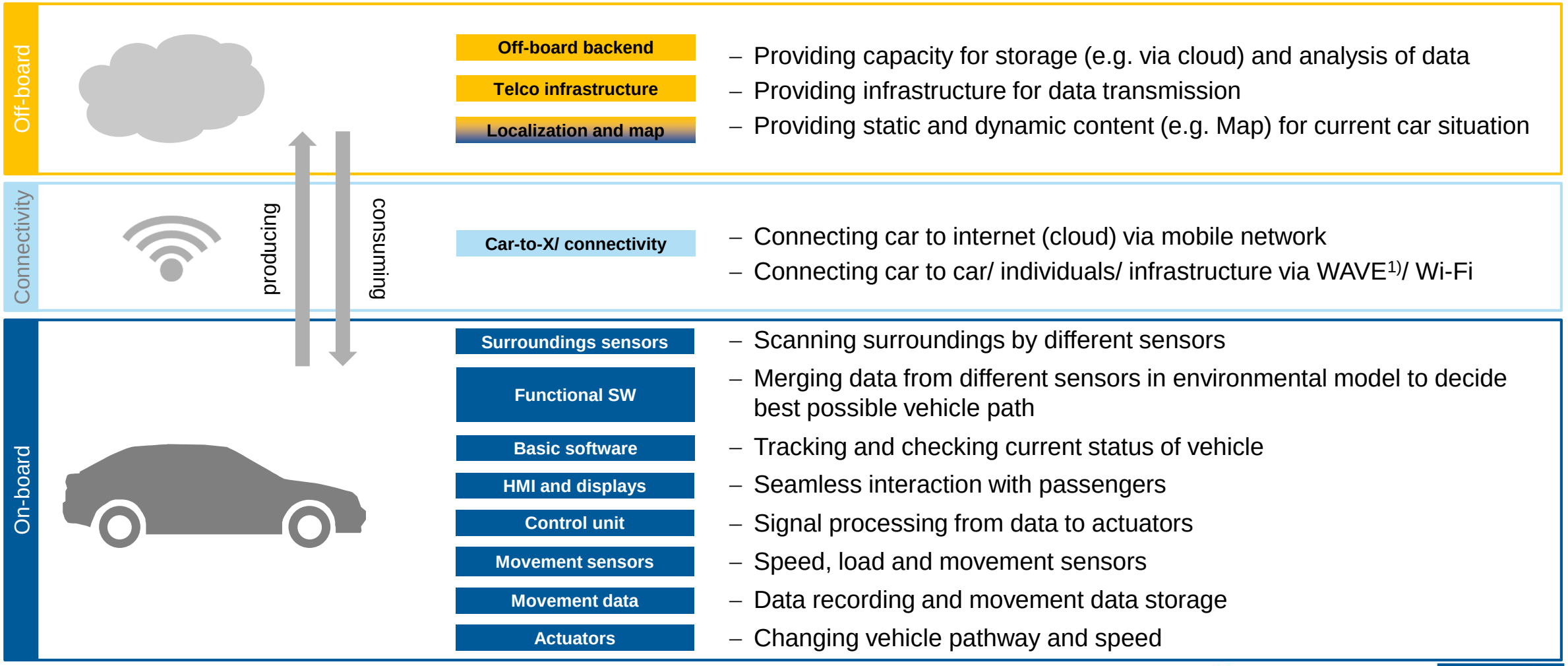
Time critical adaption of driving strategy → Ad hoc (local) connectivity:

- Vehicles communicate directly in suddenly occurring (dangerous) situations
- Indirect cloud communication is skipped for time reasons

Source: Strategy Engineers

Technologies of autonomous and connected vehicles can be divided into three clusters with several layers in each cluster

3 Technology layers of autonomous and connected vehicles

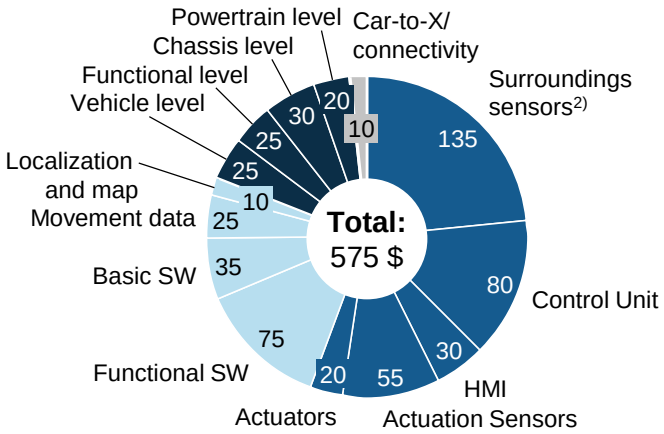


Source: Strategy Engineers // 1) Wireless access in vehicular environments, WiFi-standard exclusively for cars and infrastructure

In order to facilitate connectivity to on- and off-board systems, the total costs of car-related system is expected to rise by ca. 450% from 2016-25

2 Car-related automated vehicle value chain[1] – cost development [$/ % per car]

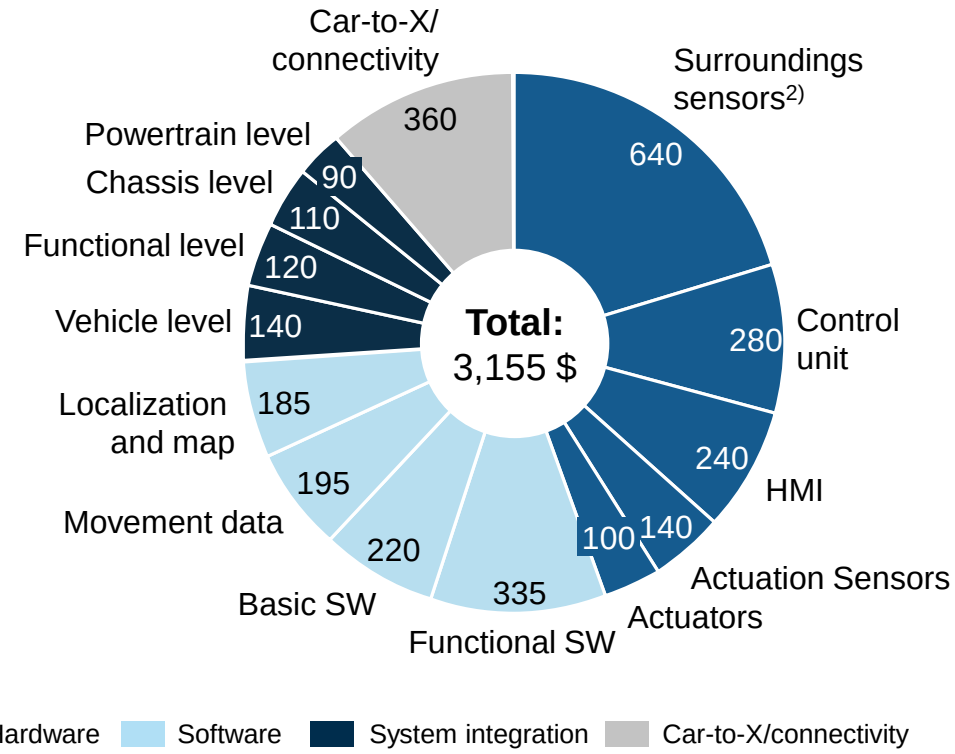
Segment costs partially automated (2016)



	2016	2025
HW[3]	320 $ (56%)	1,400 $ (44%)
SW	145 $ (25%)	935 $ (30%)
System integration	100 $ (17%)	460 $ (15%)
Car-to-X/ connectivity	10 $ (2%)	360 $ (11%)

+ 449%

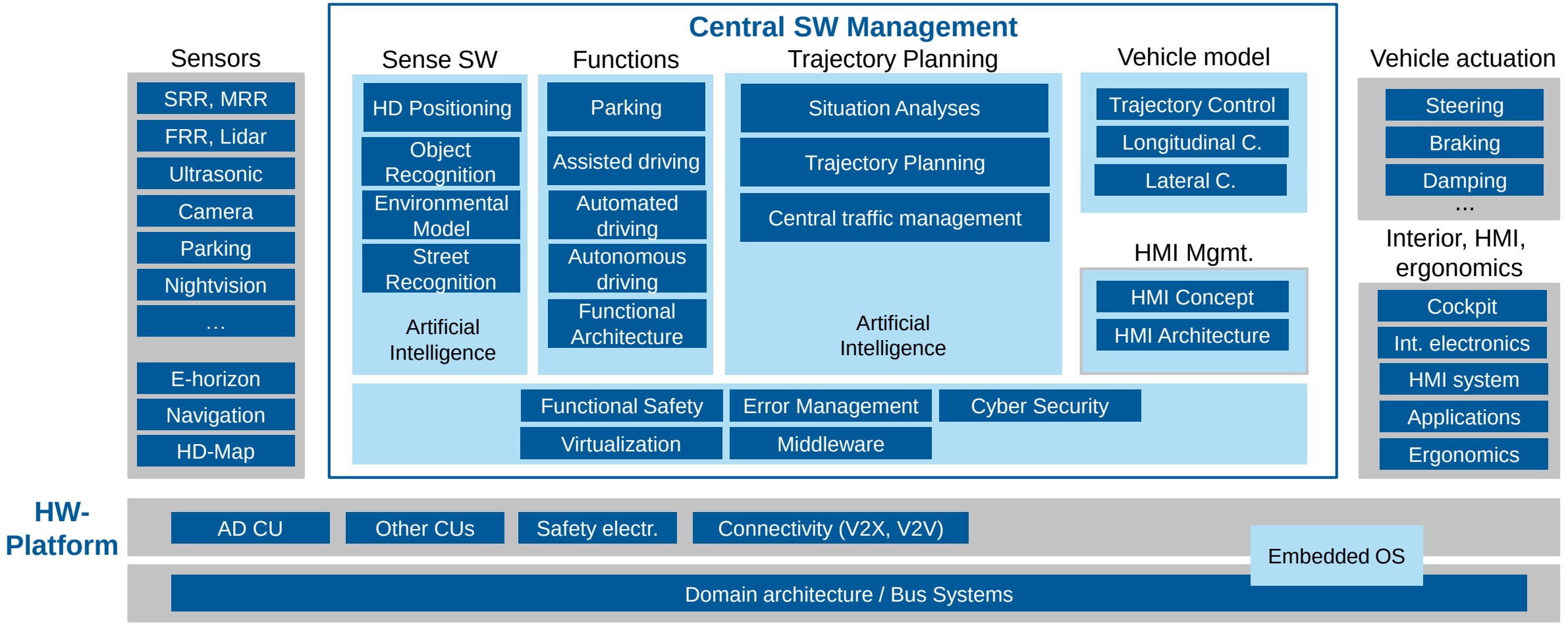
Segment costs autonomous systems (2025)



[1] Does not include off-board content (telco infrastructure, off-board backend)
[2] Sensor costs may vary strongly dependent on combination of cameras and radar (shown) vs. lidar (ca. + 335 $), [3] Hardware
Source: Strategy Engineers

Autonomous driving requires central SW management and HW platforms to interpret sensor data for path planning and automated control

2 Functional and system architecture



Source: Strategy Engineers

The resulting horizontal value chain will comprise several layers, whereas every layer will have own standards and own market leaders

2 Horizontal value chain (1/2) – Architecture-related

INDICATIVE

Suggestion for OEMs

Horizontal layers		Standard know-how	Specific know-how	Core know-how
		Buy	*Cooperation / investment*	*Internal development*
HW platform	CPU and complete ECU	▼		
Virtualisation	Special embedded kernels below operating system level for access/ functional safety requirements		▼	
Operating system	Embedded operating system, increased standardisation in the future (e.g. AUTOSAR)	▼		
Middleware	Standardisation (e.g. AUTOSAR) or quasi-standard solution	▼		
Sensor data fusion	Interface to middleware/ applications as well as data fusion mapping	▼ Interface to middleware/ applications		Data fusion mapping ▼
Sensors	Sensors incl. GPS, maps and drivers	▼		
Safety	Functional safety			▼

Source: Strategy Engineers

OEMs will need to acquire core know-how in artificial intelligence, customer-related functions, user interface and device design

2 Horizontal value chain (2/2) – Customer functions and enablers

INDICATIVE

Horizontal layers		Suggestion for OEMs	Standard know-how	Specific know-how	Core know-how
			Buy	*Cooperation / investment*	*Internal development*
Machine learning	Artificial intelligence: On-board, off-board / in cloud				▼
Applications	Perceptible benefit for the user, own applications lead to USP				▼
Connectivity	Car2Cloud, ad-hoc Car2Car as well as other Car2X		▼		
Centralised traffic control	Cloud-based route planning			▼	
Cyber Security	Data security				▼

Source: Strategy Engineers

Seven key challenges are essential for OEMs to master Level 3 to 5 autonomous driving

2 Seven key challenges for the development of autonomous vehicles

			Enabler ↔ Differentiator
Organi-sation	1. Working structure	• Project team organization, cross-functional decision rights • Agile SW development aligned with HW development	
Organi-sation	2. Vertical integration/ cooperation	• Cooperation development, management and IP rights • Alignment of diversity of geographies, time zones, company/ industry cultures and work infrastructures	
Competency clusters	3. System architecture	• Overall architecture (re-)definition and implementation • Centralized domain and CU-architecture • Modular systems (“scalability”) • Upgradeability and OTA updateability	
Competency clusters	4. Integration and validation	• Continuous integration as part of agile development • Continuous and virtual HiL/ SiL validation • Statistic/ scenario-based testing of total system	
Competency clusters	5. Functional safety and IT security	• Multi-processor HW • High priority on IT security and protection, • SW and HW protection (“security by design”) • Domain and gateway security	
Competency clusters	6. Autonomous driving functions	• AI, machine/ deep learning • 3D object recognition, data fusion • Trajectory planning (“driving strategy”) • Big data processing, Backend-based services	Crucial for competition with digitals
Competency clusters	7. HMI / User Experience	• Utilization of whole car as UI • Seamless integration of consumer electronics	

Source: Strategy Engineers

Autonomous driving functions need to become much better to gain driver's acceptance

2 ACC Comparison – Auto, Motor und Sport

Assessment





	Volvo V60	BMW X1	VW Passat	Mercedes C-Klasse	Audi A4
Scope of functions	★★☆☆☆	★★★☆☆	★★★★☆	★★★★☆	★★★★★
Precision ACC	★★★☆☆	★★★☆☆	★★★★☆	★★★★☆	★★★★☆
Precision lane keeping	★☆☆☆☆	★★☆☆☆	★★★☆☆	★★★☆☆	★★★☆☆
Handling	★★★★☆	★★★★★	★★★☆☆	★★★☆☆	★★★☆☆
Price* [€]	2,150	1,400	1,590	2,499	1,640
Total score	★★★☆☆	★★★☆☆	★★★★☆	★★★★☆	★★★★☆

Best Worst *no effect on assessment

Source: Auto, Motor und Sport

Summary

Ambiguous result

- In many situations supporting effect on the driver can be achieved
- Nevertheless, he or she always needs to be attentive
- None of the models tested could shine in all driving situations; especially lane keeping needs improvements
- Naturally, ACC functions are more sophisticated, as the have been on the market for >15 years by now
- Therefore, manufacturers' plans to release fully automated vehicles in a few year seem highly ambitious

OEMs can beat Digitals on their home turf by taking advantage of being the designer of the "vehicle ecosystem" and the integrator of all of its elements

2 Summary Autonomous Driving

- Superior autonomous vehicles will be **differentiated by their functionality and user experience**. The best vehicles will make their passenger feel **comfortable, safe and secure**
- The **future value chains will become horizontalized** and will require OEMs to make deliberate choices about where they need to build own strengths and where they rely on partners
- If OEMs want to better digital players they need to refocus and build strong competencies in the following areas:
  - **User Interface and Experience**
  - **Applications / Functionalities for autonomous Driving**
- OEMs need to be build **own core competencies** in these areas plus the following:
  - **Machine Learning / Artificial Intelligence**
  - **Sensor Data Fusion**
  - **Functional safety and cyber security**
- **All other required capabilities need to be acquired** through strategic alliances and stable supplier relationships.
- This requires **new organizational models** which ensure stringent execution and decision making. **New development processes** are needed as well as **new project management** roles and responsibilities

Source: Strategy Engineers

Riding the wave of change in the automotive industry

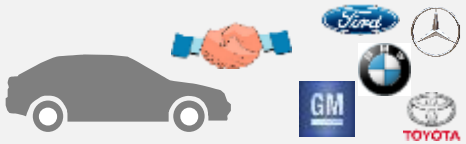
- Electrification
- Autonomous Driving
- **Digitalization**

STRATEGY ENGINEERS AVL

Digital businesses, which conveniently facilitate the use and billing of shared cars, bear the potential to disrupt the traditional automotive industry

3 Mobility business models and drivers for customer loyalty

Degree of ownership — Trade-off — Utilization & amortization

Purchase	Leasing/ long term rental	Pay-per-use/ short term rental
Focus: "Car sale/ financing"		**Focus: "Car operation"**
Single car 		**Fleet-car on demand** 
Traditional automotive business focused on <u>car ownership</u> & <u>driving experience</u>		**New businesses focused on <u>digitalization</u> & <u>purposeful mobility</u>**
<u>Few customer contact points:</u> ◆ ◆ ◆ ~ 3 years		<u>Many customer contact points:</u> ◆◆◆◆◆◆◆◆◆◆◆◆◆◆ … ~ 3 years
Loyalty through car and brand value	**Disruption potential**	**Loyalty through App, higher customer inter-action, lower cost**

◆ Vehicle sales to end-customer
◆ Service sales to end-customer

Source: Strategy Engineers

Automotive digital offers based on C2X-applications can be classified into three main clusters: “Car-integrated”, “car-related” and “beyond car”

3 Automotive digital products and services

Offers	Description
Car-integrated products and services	• **Definition:** Enrichment of the **driving experience by integrating digital content** into the car • **Examples:** Navigation, infotainment, augmented reality, mobile apps (incl. remote car control)
Car-related services	• **Definition:** (More convenient) fulfilment of customer demands **related to daily car-usage** • **Examples:** Parking services, public charging of EVs, location-based services and update/ “tuning” services (incl. remote SW-updates)
Beyond car services	• **Definition:** Fulfilment of **general mobility, social, cultural and lifestyle demands beyond customers’ own cars** • **Examples:** Car and ride sharing, intermodal travel services, event bookings/ “concierge services”

Automotive digital offers follow mobility and socio-cultural trends:
Scope goes beyond pure car-integrated products to services, which improve also non-car mobility and make life more comfortable

Source: Strategy Engineers

Basis for changing mobility needs are consumer pain points with intensifying urban traffic and eMobility limitations, e.g. parking

3 Consumer pain points

Information

- Time management
- Traffic info
- Navigation
- Delays/malfunctions
- Location search
- Choice of means of transport
- Best routes
- Navigation/Re-Routing in case of traffic jam

Intermodal Travel

- Ticketing
- Public transport
- Selection of connection
- Comfort
- Security

eMobility

- Limited driving range
- Charging station search
- High cost of batteries
- Home charging facility
- Uncertainty about EV´s conservation of value
- Uncertainty regarding EV technologies

Parking

- Parking payment
- Parking security
- Localisation of car
- Search for parking lot
- Action of parking
- Parking information

Flexible Use

- Booking
- Car sharing
- Pick up
- Car return
- Ride-sharing
- Taxi
- Help in case of breakdown

In-car | Car-related | Car-independent

Source: Strategy Engineers

The development of parking services will comprise of “aggregation” of services with cross-device support and a variety of customer segments

3 Parking market value chain and market characteristics

ILLUSTRATIVE

Traditional Parking services “Enable Parking” | **New Mobility Services “Solve the Parking Problem”**

Value Chain

Real Estate	Infrastructure	Park Mgmt.	Aggregation	Services	Devices	Customer Segments
• Parking lot	• Access Payment • Availability Detection • Reservation	• Provisioning of parking lots (based on infrastructure) incl. apps	• Sign up PSOs[1], interfaces, infrastructure for services	• Registration, Find, Prediction, Pay, Reserve • Valet Parking, LBS[2], eRouting	• Smartphone App • PND[3] • Car-integrated	• OEMs • B2B (e.g. car rental, fleets) • B2B2C (e.g. cities) • B2C

„Traditional“ Scope | **Enabler Layer** | **Scope „New Mobility Services“**

Market Characteristics

„Traditional“ Scope	Enabler Layer	Scope „New Mobility Services“
• Local / regional scope • Relatively slow deployment, complex commercial transactions • Largest share of value creation (= large gross margins) • Brand awareness not crucial • Highly fragmented market with lack of large players	• Wide coverage important • Slow deployment • Potential for cross-competitor partnering and/ or dedicated aggregator companies (e.g. “Hubject” in charging)	• Wide coverage of great importance • Fast moving competitive environment with strong importance of IT / intelligent algorithms as far as services are concerned • Long sales / implementation cycles with OEMs / B2B customers– however, can be strategic anchor points (who owns the interface between infrastructure and vehicles) • Limited margin potential on services revenues • Brand awareness important in case of direct B2C acquisition (less important with B2B / B2B2C sales) • Most likely strong consolidation expected in the future (especially with regards to social / shared offerings)

Source: Strategy Engineers Research // [1] parking space operators, [2] location-based services, [3] personal navigation device

„Future parking“ is an innovative topic area with different players who can boost unexploited potentials by collaborating

3 Automated parking: Players and products

ILLUSTRATIVE

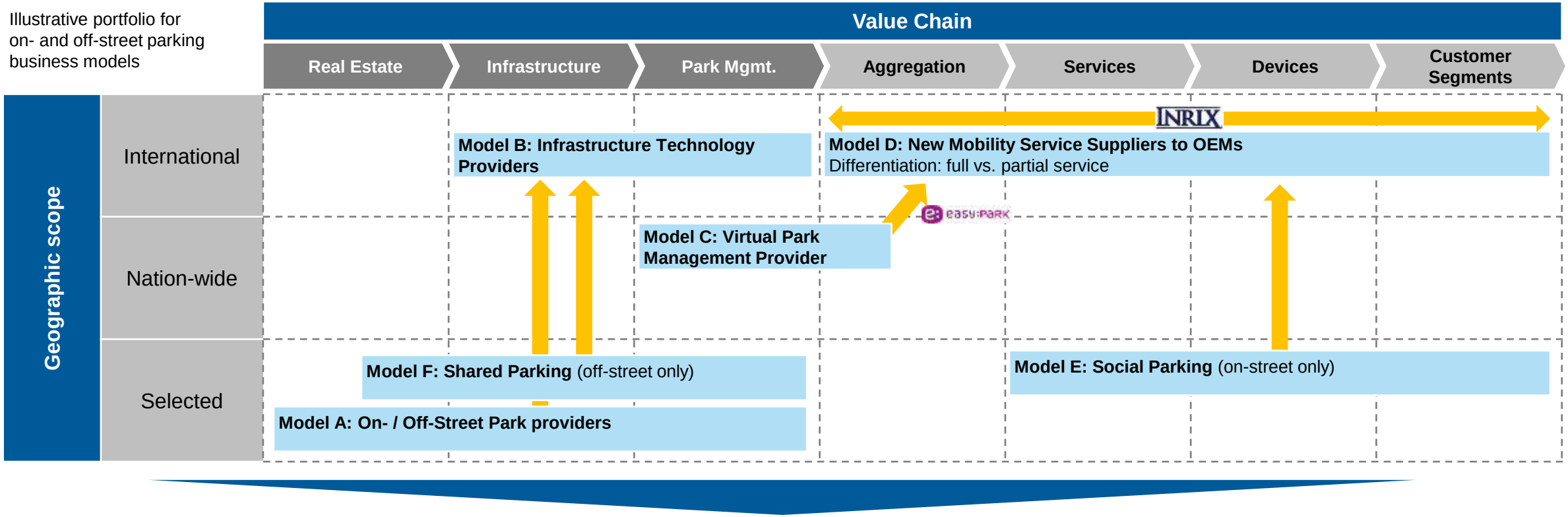
	Real Estate	Infrastructure	Park Mgmt.	Aggregation	Services	Devices	Customer Segments
	Conventional extents			„Enabler“	New services parking, mobility, „Big Data“		
Companies	GOLDBECK, HUBER	LODIGE INDUSTRIES, serva, NAVVIS, SIEMENS, PARK HERE, BOSCH	APCOA PARKING, CONTIPARK Interparking Group, empark Interparking, Conv. Valet Parking	easy:PARK, Parkmobile, INRIX, ParkNow	SMART PARKING, gottapark, TraviPay, ParkMe	BMW, Audi, DAIMLER, HYUNDAI, Volvo, Volkswagen, Continental, Valeo	B2C, B2B2C, B2B, SIXT, Europcar, DriveNow
Products/ services	• Planning and (re-)building parking garages/ -spots • Maintenance of the property	• Fully automated parking robots • 3D-indoor maps • Sensors for parking spot localisation • Devices for vehicle authentication and billing	• „House-Keeping“ • Capacity-management • Season tickets, club offerings etc. • Accounting and billing • Conventional valet parking	• Automated merging of various services • Creation of a critical mass and (data-) standards via pooling of single or regional services	• „Exploitation“ of infrastructure and community • Localisation of parking spots • Price compa-rison of spots, reservation • Autom. Entry and exit in car parks and payment	• Connection with infrastructure/ digit. services / data transfer • Cameras, sensors, displays in car • Planning/execu-tion of drive/ park strategy • App integration into car	• „Exploitation“ of in car data • Location-based Services • Pilot/ isolated solution for fleet provider:. Automated parking in geographically limited areas

Source: Strategy Engineers

Various business models have established / arisen along the value chain with strong dynamics to expand / alter focus of value creation

3 Scope of different business models for on-/off-street parking services

ILLUSTRATIVE



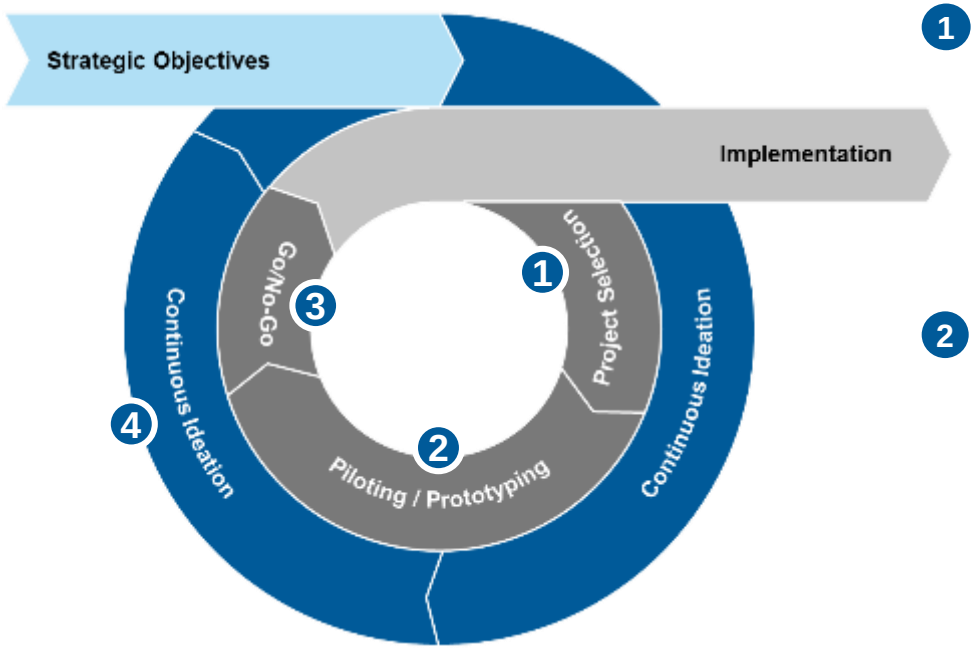
- Business model analysis: How do the key players in the industry position themselves?
- Potential: identification of blue ocean scenarios, anticipation of future developments

Source: Strategy Engineers Research // ➡ expected future development

The definition and piloting of strategic initiatives at level 3 is the heart of the agile digital strategy processes, enabling quick and decisive actions

3 Level 3 – Strategic Initiatives: Process

Agile strategy development process ("TurboCharger")



1 Project Selection

- Strategy and new product linkages
- Governance of new initiatives
- Tracking and definition
- Project approval decision-making processes
- Use of advanced valuation methodologies

2 Piloting, Prototyping

- Disciplined and effective stage/ gate process
- Time to market
- Bottleneck elimination and identification of project "congestion"
- Parallel planning of work steps
- Resource allocation

3 Continuos Ideation

- New product and technology ideas
- New business concepts and opportunities
- Consumer insights
- Trend analysis and anticipation
- New to the world and extensions of existing ideas

4 Go/No-Go

- Marketing and investment planning
- Consumer profiling and segmentation
- Competitive response and timing
- Advertising and promotion decision-making
- Product tracking

The strategy TurboCharger …

… is an agile process
… is a continuous process
… uses parallel processes
… utilizes frequent and short review cycles
… is driven by short decision intervals
… builds a back-log of initiatives
… re-assess and re-prioritizes activities/back-log frequently and rapidly

Source: Strategy Engineers

Riding the wave of change in the automotive industry requires to reinvent the way cars are made, new types of cars and new businesses

1 3 Summary

1 Starting point: Take stock, prepare and enable

- Describe company vision and direction for new value creation
- Discover existing value creation areas
- Develop ideas about new value opportunities
- Set new value business case framework
- Develop and approve action plan

2 New carmaking

Optimize within current boundaries

- Scan entire supply chain for new value opportunities
- Investigate sustainability along entire value chain
- Maximize scale in components and systems
- Adjust footprint to global business requirements (Locations, Organization, Processes, etc.)
- Increase process efficiency (throughput) in planning, engineering, and purchasing

3 New cars

Plan, engineer, launch new vehicle types

- Accelerate simultaneous development cycles
- Decouple vehicle and electronics development cycles
- Improve trade-off decisions between weight – cost – performance to reduce weight
- Improve planning decisions balancing regional requirements and global standards
- Investigate mission and country specific derivatives

4 New business

Enter and excel in new business areas

- Drive extended value creation through new usage models for cars (Energy storage, rental, etc.)
- Use connected car models for partnering with service providers
- Increase service sales
- Install corporate ventures
- Enhance partnering with suppliers and dealers

Source: Strategy Engineers

Questions?

STRATEGY ENGINEERS member of the AVL Group AVL

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Four years in a row!

Once again after 2014, 2015 and 2016 Strategy Engineers has been awarded as “best consultants” in 2017 by German leading business magazine brand eins and Statista. In addition to an improvement within the three categories “automotive & supplier”, “machinery & plant engineering” and “operations management”, Strategy Engineers was ranked for the first time as best consultant in the category “strategy development”.

This statistical evaluation was conducted by Brand eins and Statista on the performance of 15,000 consultancies in total. With more than 3,200 questioned clients, executives, project leaders and partners this survey represents the biggest one within the German consultancy market.

Source: Strategy Engineers, brand eins