

## Captive Auto Insurances

*an Untapped Downstream Profit Potential for Car Manufacturers*



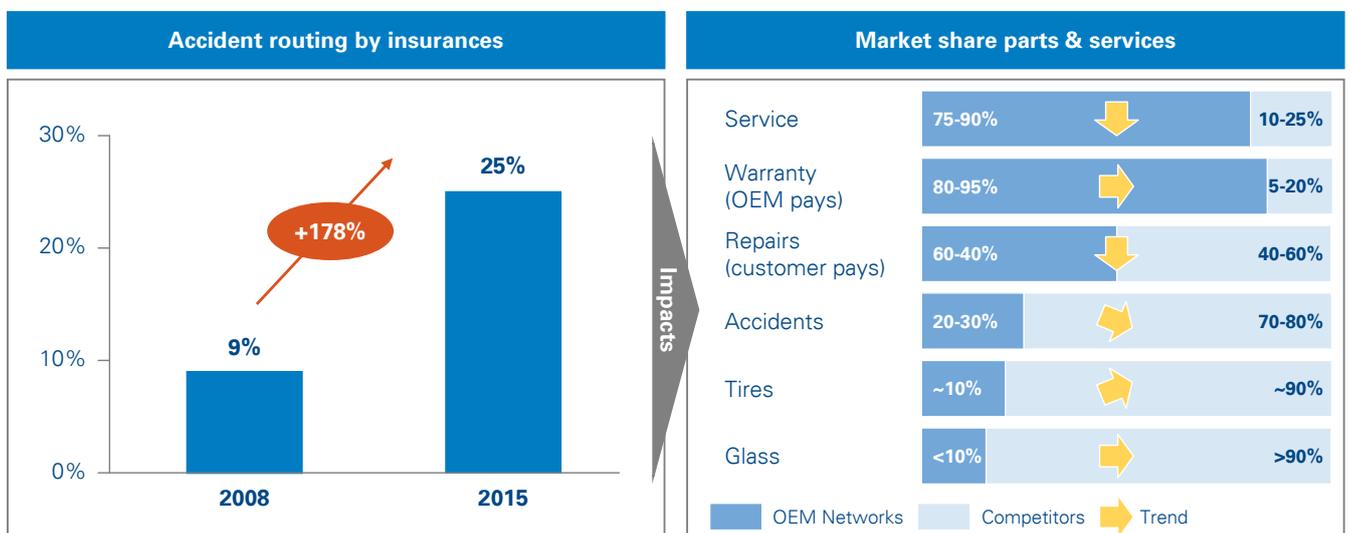
Parts and Service remain the largest profit generators for car manufacturers. This substantial high margin business has attracted independent low cost repair shop networks, which have increasingly become preferred supplier to car insurers who are striving to keep costs at bay. Most automotive OEMs have started to counter this business drainage by pushing their own label insurance products into the market – however, the results so far leave room for improvement.

### The need to prevent further erosion

Independent car insurers keep professionalizing and optimizing their claims management not least by routing accidents to their preferred supplier repair shops. On top of that they are issuing more and more insurance products with binding repair shop regulations. Research suggests that by 2015 every fourth car police will include a statute on where to repair accidents (see figure 1).

While it is a commonly known fact that OEM-network usage for car repairs and accidents is decreasing with car age, these days we observe that increasingly even cars younger than four years are routed into independent networks. This trend further decreases the OEMs market share from today approximately 25% of cars to 15% or even less within the next five years. In other words: more than three-quarters of this highly profitable business is lost. Studies claim that the car industry generates ~20% of its revenues in aftersales, generating ~50% of the

Figure 1: Accident routing



Source: DAT, Arthur D. Little

profits. This source of substantial profits must not be neglected or run half-heartedly. Therefore, to prevent further erosion, many OEMs already cooperate with insurance companies and provide their own-labelled insurance products to their customers. However, they still fall short to penetrate cash buyers or the used-car market with their captive insurance products, hence giving away millions of Euros in insurance commissions and – of course – revenues and profits from parts and service fees.

### Captive insurance distribution – an as-is assessment

Arthur D. Little has recently conducted a study analysing the product specs, pricing, promotion and the sales process of captive insurance products across the leading car OEMs dealerships in Europe’s key markets. Despite the underlying multi-layer profit potential the business practices discovered in the study were rather devastating across all makes and markets.

#### Product

OEM insurance products include several interesting car-related bundles that cannot be found in products of independent car insurers. Our study shows that the product and service portfolio is rather homogeneous across makes and markets, so still there remains a major potential for further product and service innovation to differentiate even further. In particular additional premium services that are closely related to the core product ‘automobile experience’ and the respective make are not fully exploited yet. The highly emotional experience ‘car’ is only insufficiently covered by the available insurance packages (see Figure 2).

#### Price

The product bundles provided by the OEMs are difficult to compare with standard car insurances, hence a price comparison has to be carefully evaluated if it is possible at all. However, as OEM’s car insurance premium cover products cost of often more than twice the price of a standard comprehensive coverage insurance policy, an immediate sense of over expensiveness seems unavoidable. Only few sporadic “Young Drivers” products offer an obvious pricing advantage in comparison to independent insurances, supposedly by subsidizing the insurance premium out of the car and aftersales profit margins.

#### Place and Promotion

While internet applications for car configurations are highly sophisticated, including real-time leasing and financing calculations, insurance quotes are not integrated. As a matter of fact, even stand-alone insurance premium calculators can only be found on very few of the OEM websites. When trying to find information on the insurance products, the potential buyer needs to navigate through numerous links that are often difficult to find to begin with. When finally having called up the insurance brochures, the information provided is often incomplete, inconsistent or simply confusing. In some countries, an interested user will only find a bland note that information on insurance can be found on some insurance company’s webpage. While the information about car insurance on the webpages of automotive manufacturers is scarce, it is completely absent at their car dealerships. With the exception of one dealership, no posters, leaflets or booklets on insurance products could be found anywhere with any make and in any country.

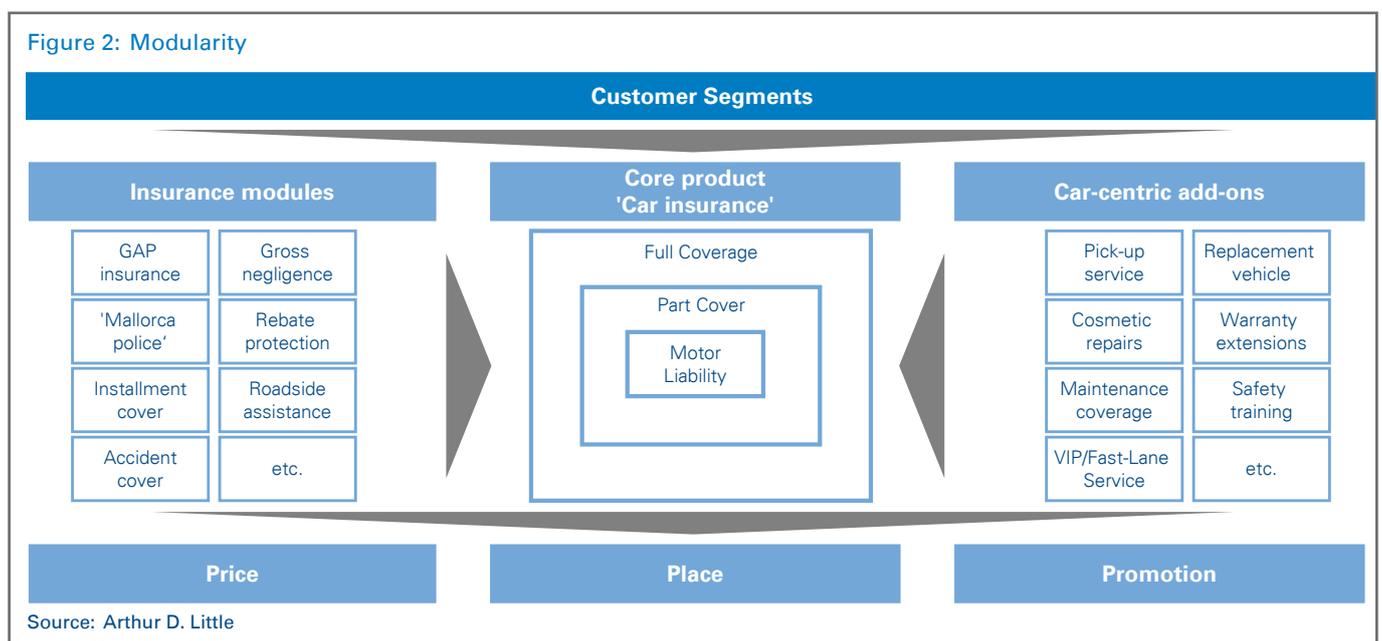


Figure 3: Expertise at dealerships

Area of Expertise												
Expertise Financing	63,5	66,1	63,1	63,8	53,9	54,2	61,3	51,1	53,8	59,5	60,5	63,3
Expertise Leasing	54,0	52,0	46,8	42,1	33,3	38,6	35,1	31,2	48,0	40,4	40,4	53,2
Expertise Insurance and other additional services	22,8	33,6	44,0	53,9	23,9	26,8	52,8	24,2	31,2	34,4	23,6	42,8
Market insight financial service products	50,3	49,7	48,9	51,5	42,9	41,2	55,5	36,5	43,4	50,2	47,9	60,5

Source: Automobilwoche – Distribution in Germany Special 2010 (Top score = 100)

### Process and People

During Arthur D. Little's study, sales personnel across makes and markets was rather reluctant to sell insurance products, particularly when the car in question was supposed to be paid for in cash. None of the sales persons suggested an insurance product unsolicited. They only discussed the products on request, and even then they usually only presented warranty extensions. When being asked about comprehensive coverage products, they had very little product knowledge and were explicitly expressing their lack of confidence in the product perse. On numerous occasions this resentment went to an extend where the sales person suggested to rather buy an insurance product from an independent provider because of its superior value for money than the own product. This lack of expertise can be found across all major car manufacturers dealerships (see Figure 3).

### Innovative ways to overcome the barrier

While some of the above shortcomings can be explained with legal restrictions and regulations on insurance distribution in some European markets, an innovative approach is required to increase insurance penetration and claim the lost profit potential. Arthur D. Little suggests a lean, yet comprehensive approach (see figure 4) to increasing insurance penetration based on its High Performance Business Model™ methodology and toolbox, resulting in an increased routing of repairs into the own shops. To optimize the effort, 3-5 pilot markets need to be selected e.g. based on their size and/or growth potential. For these markets, customer requirements are assessed. Gaps between buyer needs and services provided by the OEM insurance product are identified quantitatively and qualitatively. Based on this comprehensive gap analysis, product design and pricing are redesigned to better match the market's requirements. Subsequently product presentation and promotion is redefined to increase the level of available

Figure 4: Comprehensive approach



Source: Arthur D. Little

information for the potential customer. These steps include an in-depth cooperation with the risk carrier and are facilitated by Arthur D. Little's network of industry experts from the automotive as well as the insurance industries. In order to achieve sustainable improvements, the sales personnel needs to understand the insurance products better to feel more comfortable to convincingly integrate them into the sales process. Furthermore sales personnel needs to understand the long-term benefits of insurance products in their respective market share of aftersales as well as the effect on customer loyalty. Usually the monetary and non-monetary incentive systems will have to be adjusted to further push the efforts. However, Arthur D. Little's experience shows that there is no one-size-fits-all solution. The global markets legal and cultural specifics need to be reflected thoroughly.

### Conclusion

Increasing insurance penetration offers substantial volume and profit potential from commissions, parts and services. So far, OEMs struggle to route this business in their own shops and realize the substantial underlying profits. Particularly in the cash buyer and used car segments the current situation shows substantial improvement potential. Today OEMs are losing millions of Euros in each year to insurance and independent repair network competition. Based on its in depth understanding of the automotive and the insurance business, Arthur D. Little offers a lean but comprehensive methodology to innovatively increase market share in the highly lucrative downstream business globally.

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### Arthur D. Little

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