
Automotive Industry:

Five leadership Issues Worthy of Board and Executive Attention

Introduction

Changes in consumer demographics, consumer habits and technological advances are forcing the automotive industry to change dramatically. Driving innovation across the organization, digitization, partnering—whether through joint ventures or mergers and acquisitions—and a host of other major risk drivers all are contributing to dialogues in boardrooms and executive offices. Most significantly, executives are asking if they have the right leadership talent in light of the challenges they face.

From our conversations with board members and CEOs in the automotive industry, the following five issues and their implications on leadership talent have emerged as top of mind for the executives:

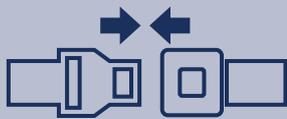
- Nurturing innovation throughout the entire company
- Capitalizing on digital disruption
- Partnering for success
- Identifying next-generation leaders
- Creating a diverse and engaged board

We hope this executive briefing document will serve as a discussion starter for thinking through how to attract and retain the right leadership talent in the face of these challenges.

Nurturing Innovation Throughout the Entire Company

- Changes in consumer demographics, consumer habits and technological advances are forcing the automotive industry to change dramatically.
- It is more important than ever to focus on innovation capabilities at every level of the company, not just R&D and engineering, and to develop or acquire the talent needed to lead in this period of transformation.

AUTOMOTIVE COMPANIES ARE RESPONDING TO MARKET CHANGES, BUT HAVE THEIR TALENT STRATEGIES CAUGHT UP?

| | Attracting Customers | Non-Buying Habits | New Hazards |
|-------------------|--|---|---|
| Market Then |  <ul style="list-style-type: none"> ■ Only 2.3% in online advertising was spent on automotive in 2001.^A ■ 7 visits were made to the showroom before buying a car compared with today's 1.5 visits.^B |  <ul style="list-style-type: none"> ■ Car ownership was a cultural symbol of individual freedom and status. ■ Second largest: On average, the car is the second most expensive discretionary purchase after the home. |  <ul style="list-style-type: none"> ■ Minimising injury to passengers is the core of carmakers' safety offerings, with new safety records year after year. |
| Market Now |  <ul style="list-style-type: none"> ■ 92% of customers visit at least 6 websites before buying a car.^C ■ More than a third of customers would consider buying a car online.^D |  <ul style="list-style-type: none"> ■ Sharing economy: Financial reasons are deterring younger generations from buying, while plentiful supply has popularised carsharing as an alternative to full-time ownership. |  <ul style="list-style-type: none"> ■ Securing data: Passengers expect improved cybersecurity and protection of their personal data in the increasingly connected car. |
| Company Responses |  <ul style="list-style-type: none"> ■ 35% in mobile advertising was spent on automotive.^E ■ Online sales trials have been made by Autohome, Dacia, Ford and Volvo.^F |  <ul style="list-style-type: none"> ■ Selling a mobility plan: Carmakers are exploring flexible-use offerings such as Audi unite, BMW's DriveNow, Daimler's Car2Go, Toyota's Ha:mo and GM's project with the Chinese government.^G |  <ul style="list-style-type: none"> ■ A binding promise: In 2014, 24 carmakers jointly signed a pledge to protect customer data privacy in their vehicles.^H |

KEY POINTS

- Develop innovation capabilities in every part of the company, including marketing, sales, design, production and distribution.
- Invest in employee incentive systems that encourage experimentation and the development of new ideas.
- Establish a dedicated career path for innovation leaders and groom critical competencies early on such as entrepreneurship, broad business acumen, strong drive for results and timely decision making.
- Acquire new capabilities in the domain of online, mobile, Big Data analytics and cybersecurity.

Capitalising on Digital Disruption

- Digital is impacting the entire automotive value chain from point of design to engineering and production to sales. It is facilitating communication like never before among manufacturers, consumers and their cars.
- The automotive industry will require digitally literate and deeply innovative talent at executive levels to match the pace and nature of this disruptive transformation.

DIGITAL IS INCREASINGLY UBIQUITOUS ACROSS THE AUTOMOTIVE VALUE CHAIN

SHARED SERVICES (Digitised Finance, HR and other support functions)

ENGINEERING AND DESIGN

At General Motors, social media chatter on vehicle performance is funnelled straight back to the Engineering Department to improve future products.^A

PRODUCTION

BMW currently is trialling Google Glass and video streaming in vehicle quality control processes.^B

MARKETING

In 2013, Twitter drove \$716 million in auto sales through Twitter ads, positive brand mentions, amplification of TV advertising and automakers' own Twitter activity.^C

SALES

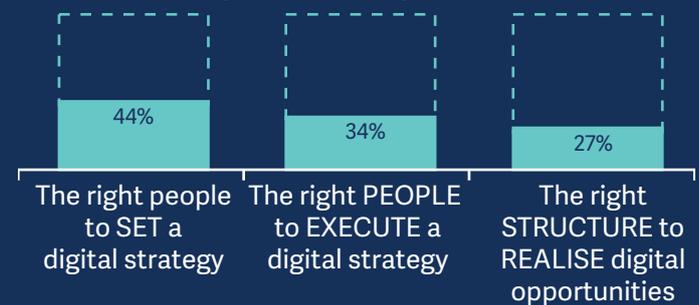
Audi's refurbished Mayfair showroom in London has only 4 physical cars and features digital display walls. Sales have increased 60% as a result of the transformation.^D

AFTERSALES

83% of consumers use a smartphone to find the location of the nearest service centre.
63% of consumers would use a tablet device to research aftersales prices.^E

A MAJORITY OF AUTOMOTIVE EXECUTIVES THINK THEY DO NOT HAVE THE RIGHT TALENT AND STRUCTURE TO SUCCEED IN DIGITAL TRANSFORMATION^F

% respondents say their company has ...



LACK OF DIGITAL SKILLS AND NON-SUPPORT BY LEADERSHIP ARE KEY BARRIERS^F

The three most significant leadership barriers to effective digital business according to industry executives:



Lack of digital expertise or digital skills



Digital not seen as important by leadership



No single head of digital

THE BEST POTENTIAL LEADERS ARE THOSE WITH TRANSFORMATIONAL—NOT JUST DIGITAL CHANGE—COMPETENCIES^G

LEARNING AGILITY

WILLINGNESS TO TAKE CALCULATED RISKS

CONFIDENCE TO GO AGAINST THE GRAIN

ENTREPRENEURIAL SPIRIT

LEARNING AGILITY

KEY POINTS

- Identify and nurture talent within the company who exhibit the ability to drive disruptive transformation.
- Consider recruiting from outside the automotive industry, especially from the technology and consumer sectors.
- Explore the opportunity to form a Technology Advisory Board that can counsel on the company's course towards the digital future.

Partnering for Success

- The automotive industry is changing rapidly, and individual companies cannot build all the necessary capabilities fast enough to keep up. As a result, partnerships of various forms are on the rise and it is important to create structures that foster equality.
- Companies must apply due diligence beyond numbers in order to create lasting value from the partnerships, and there is a growing need for talent who are able to identify opportunities and manage integration.

AUTOMOTIVE SUPPLIERS ARE SEEKING TO SCALE THEIR CAPABILITIES IN RESPONSE TO INCREASING PRESSURE FROM OEMS^A

USD\$27.5 billion

total deal value in 2014 H1, the highest in the last seven years

110% increase

in total deal value compared with 2013 H1 in the first half of 2014 alone

66% increase

in average automotive deal size in the same period

SEVERAL AUTOMOTIVE INDUSTRY CHALLENGES CALL FOR CAPABILITY ACQUISITION THROUGH PARTNERING

DIGITAL TRANSFORMATION

Partnering to acquire digital capabilities

ENTRY OF NON-TRADITIONAL PLAYERS

Partnering to win in new technology and services

CHANGING NEEDS OF CUSTOMERS

Partnering to gain insight into customers' future

LOCAL DIFFERENTIATION

Partnering to gain access to local talent and insights

THERE IS A HIGH RATE OF FAILURE IN M&A DUE TO POOR CULTURE INTEGRATION

50%

of M&As fail to create value^B



75%

of JVs end within 2 years of formation^C

Possible sources of cultural mismatch include:

| | |
|------------------------|--|
| PACE OF CHANGE | Agile vs. controlled |
| STRUCTURE | Flat vs. matrixed |
| | Focused siloes vs. integrated whole |
| REGULATORY ENVIRONMENT | Highly regulated vs. easily navigable |
| NATIONAL CULTURE | Eastern, Western or other strong cultural influences |
| STRATEGY | Need for a single agreed vision |
| EXPECTATIONS | Directive vs. equal partnership |

THERE ARE MANY RECENT EXAMPLES OF PARTNERING IN THE INDUSTRY

MERGERS & ACQUISITIONS



JOINT VENTURES



ALLIANCES



TALENT REQUIREMENTS FOR SUCCESSFUL PARTNERING

1. Skillful management of effective cultural integration
2. Talent with strategic ability to spot opportunities
3. Clear road map for leadership integration and communication
4. Strong governance frameworks

KEY POINTS

- Exercise due diligence beyond number crunching in selecting a partner and develop internal capabilities to foster equal partnerships.
- Consider bringing in a third party to identify desired culture and to assess future fit with the prospective partner.
- Leverage best practices from each organisation and invest in maximising each partner's competencies going forward.

Identifying Next-Generation Leaders

- Future automotive executives will be doing business in a very different industry from the one we know today. Companies need to think about executive profiles, which will enable them to thrive in as-yet unknown markets.
- Promotions based on tenure can backfire in a global market that values agility and lateral thinking, especially if done without proper benchmarking of comparable talent in the market.

THERE IS LITTLE DIVERSITY AMONG SENIOR AUTOMOTIVE EXECUTIVES TODAY; THEY TEND TO BE MALE AND OF THE SAME NATIONALITY AS THE COMPANY HEADQUARTERS, WITH ABOUT 15 YEARS IN THE COMPANY AND ALMOST AN ENTIRE CAREER WITHIN AUTOMOTIVE^A

| OEM Executive Profile | 5% | 30% | 30% | 20% | 43% | 15 years |
|---|---|---|---|---|---|----------|
|  |  |  |  |  |  | |
| Female | Foreigner* to HQ | External Recruits | Recruits from a Non-automotive Company | Foreign Experience | Average Years Spent with Company | |
| Tier 1 Executive Profile | 9% | 27% | 27% | 40% | 54% | 16 years |

AUTOMOTIVE CEOs ARE LARGELY INTERNAL APPOINTMENTS AND "COMPANY LIFERS"^A

| 2% | 16% | 60% | 13% | 8% | 60 years |
|---|---|---|---|---|---|
|  |  |  |  |  |  |
| Female | Foreigner* to HQ | "Company Lifers" | External Recruits | Recruits from a Non-automotive Company | Average Age |

THE INDUSTRY HAS ACKNOWLEDGED THE NEED FOR A NEW TYPE OF LEADER - BUT IS IT ACTING ACCORDINGLY?

"Carmakers need a younger generation with 'creative energy' "

Stefan Quandt, Deputy Chairman, BMW^B

THE NEW CRUCIAL COMPETENCIES FOR AUTOMOTIVE LEADERS

- Decisive and resilient
- Excellent track record in operations
- Socially adept
- Experience in disruptive markets/companies
- Digital experience

KEY POINTS

- Actively review your employee value proposition not only against automotive peers but against industries that could be tomorrow's talent pool.
- Consider bringing in talent from outside the industry who can bring with them innovative skills and experience to help the company succeed in the face of disruptive innovation.
- Look for diverse candidates in terms of gender and international experience to improve the diversity of perspectives in the company.

Creating a Diverse and Engaged Board

- An effective board is one that represents a rich variety of perspectives, allowing companies to develop (and execute) robust strategies while simultaneously managing risk.
- The work of the board has never been more complex as traditional issues remain important while new challenges arise.

| TRADITIONAL CONCERNS FOR BOARDS | | | NEW ISSUES REQUIRING BOARD ATTENTION | | |
|---|---|--|--|---|--|
|  Regulations |  Logistics/ Supply Chain |  Green/Eco |  Digital |  Non-traditional Buying Patterns |  Shareholder Activism |
|  CEO Succession |  Remuneration | |  Partnering |  New/Emerging Markets |  Cybersecurity |



AUTOMOTIVE BOARDS ARE NOT DIGITAL-READY^A

1 DIRECTOR WITH DIGITAL EXECUTIVE EXPERIENCE among 230 directors surveyed

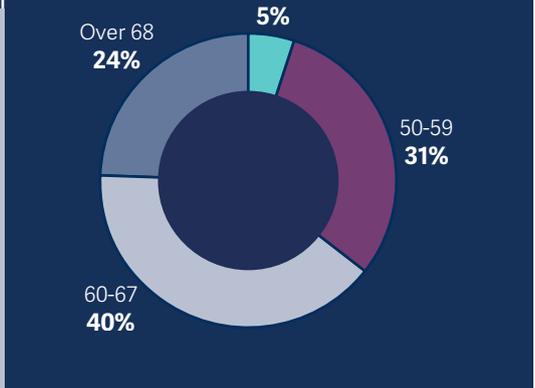
AUTOMOTIVE BOARDS HAVE LITTLE GENDER DIVERSITY^A

85% **15%** This is despite the fact that women have a strong influence on car buying decisions.




TWO-THIRDS OF AUTOMOTIVE BOARD SEATS COULD TURN OVER IN THE NEXT FEW YEARS

Automotive board composition by age^A



- ### KEY POINTS
- Conduct regular director and board evaluations—this will help ensure that director performance is aligned with the company’s strategic objectives.
 - Focus first on the capabilities, experience and perspectives necessary to provide agile oversight, effective corporate governance and appropriate counsel to the senior executives.
 - Look for candidates with digital experience or consider forming a Technology Advisory Board to help the company prepare for the future.

Endnotes

NURTURING INNOVATION THROUGHOUT THE ENTIRE COMPANY

- A "Auto Manufacturers Spend Billions Marketing SUVs to American Consumers", Public Citizen, 2003;
"The Decade in Online Advertising," Double Click, 2004
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- C Rohan Samson, M.D., et al., "Impact of Online Digital Communication on Customer Buying Decision" survey, Accenture, 2014
- D "Innovating automotive retail", McKinsey & Company, 2014
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- F "The Future of Car Retailing," *Forbes*, 2014;
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- G "Carsharing gets creative with new programs from Audi, Toyota," JWT Intelligence, 2014
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CAPITALISING ON DIGITAL DISRUPTION

- A "GM executives help scour social media to spot vehicle flaws", *Automotive News*, 2014
- B BMW AG press release, November 2014
- C "Study: Twitter Marketing Drives \$716 Million in Car Sales", *Advertising Age*, 2014
- D "Audi makes London showroom a tech-rich showpiece for the brand", *Automotive News*, 2014
- E "Four ways dealer groups can beat independents on digital aftersales", *AMOnline*, 2014
- F *Digital Pulse Survey*, Russell Reynolds Associates, 2015
- G Proprietary research, Russell Reynolds Associates, 2015

PARTNERING FOR SUCCESS

- A "Global Automotive M&A Deal Value increased to \$27.5 billion, a strong increase of 110 percent over the first half of 2013", PwC, 2014
- B "Practice Makes Perfect: Mergers & Acquisitions", Oliver Wyman, 2014
- C "The Science of Alliances", PwC, 2014

IDENTIFYING NEXT-GENERATION LEADERS

- A Automotive study of 210 executives at the world's top OEM brands and Tier 1 companies by revenue, Russell Reynolds Associates, 2015. "Company lifers" are executives with over 15 years of employment with the company.
- B "BMW's designated CEO Krueger will usher in new era at automaker", *Automotive News*, 2015
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CREATING A DIVERSE AND ENGAGED BOARD

- A Automotive study of 230 board directors on the boards of the world's top OEM groups and Tier 1 companies by revenue, Russell Reynolds Associates, 2015
- B "Secure tomorrow's car buyers today", global automotive demand report, The Nielsen Company, 2014

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