

# Improving Cost Management in the Automotive Supplier Industry

**A new Capgemini study uncovers four key levers that offer automotive suppliers potential for significant cost reduction.**

In recent years, intense competition in the automotive supplier industry has resulted in significant changes to the landscape, with the emergence of new markets and new players. In this challenging environment, effective cost management has become imperative in order for suppliers to maintain profitability.

Yet, despite a growing emphasis on cost-reduction initiatives, Capgemini's research over the past several years indicates a lack of true progress in the area of cost management. This raises an important question: Is the automotive supplier industry using the correct levers to reduce costs efficiently and effectively?

Our new study, "Cost Management in the Automotive Supplier Industry," is designed to answer this question

by examining the impact, causes and interrelationships of key cost drivers. The research was conducted by Capgemini's Automotive Center of Excellence in Stuttgart, Germany, and included interviews with executives of more than 20 leading tier 1 automotive suppliers. In particular, we looked beyond traditional expense categories such as finance/controlling, purchasing/supplier, manufacturing and HR/administration. For many companies, these cost-management levers have brought short-term benefits but are already optimized.

Instead, the research examined four cost categories that until now have been overshadowed: customer, innovation, product and globalization.



## Uncovering New Levers for Cost Savings

The extent of influence and the impact of each lever was analyzed. And within each cost category, specific cost drivers were studied.

**Customer:** Suppliers are faced with the challenge of fulfilling strict OEM requirements relating to quality and flexibility as economically as possible. Response to demand fluctuations and an increase in efficiency in the sales process are growing issues for suppliers. The research found that 90% of automotive suppliers incur costs of up to 7% of sales due to flexibility requirements for delivery schedules. Additional cost drivers include customer acquisition and loyalty.

**Innovation:** Every development and introduction of an innovation must be considered with an eye toward the cost factors. For example, product or process innovations can provide companies with price

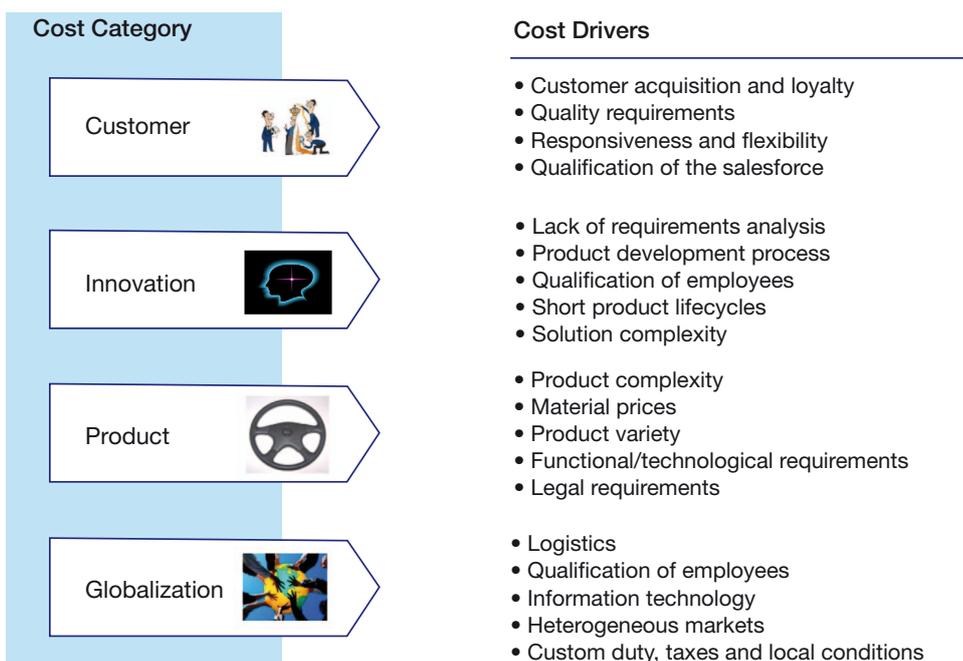
or cost advantages through short-term monopoly positions. At the same time, innovations can involve high costs and hold the risk of bad investments when there is a lack of market acceptance. In many cases, a significant share of the supplier's investment in innovations cannot be translated into sales or market share. Cost drivers related to innovation include lack of requirements analysis, accelerated product development process, qualification of employees, short product lifecycles and solution complexity.

**Product:** To a large extent, product requirements are influenced by the customer and the relevant legislative bodies. Technical/functional requirements as well as legal regulations, particularly related to environmental protection, are important cost drivers. The majority of companies surveyed in our research are confronted with an increasing range of product variants, a growing cost factor for many

suppliers. This has made it difficult to achieve planned targets related to time schedules, costs and quality in production start-ups. Technical complexity is an additional cost factor that is growing in importance due to the increasing number of electronic components.

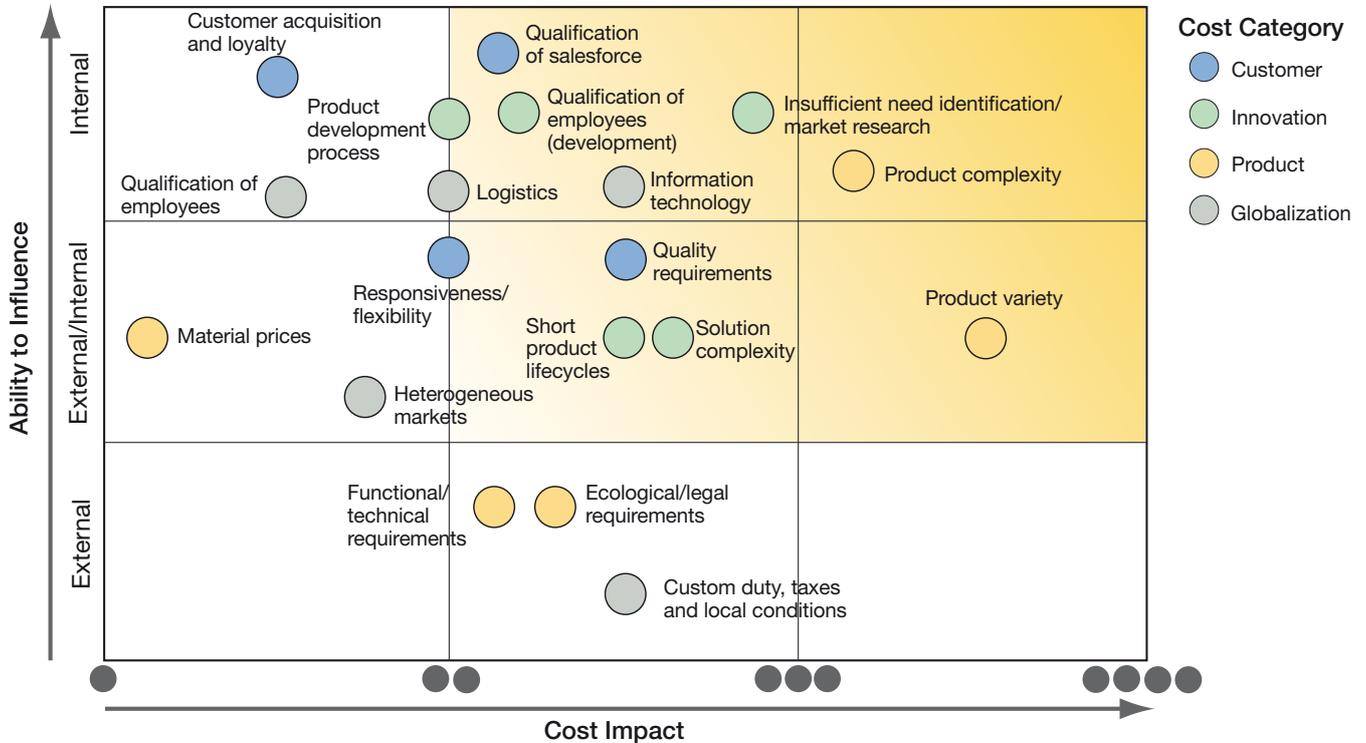
**Globalization:** Companies are beginning to discover that rising supply chain and logistics costs stemming from global supplier networks can partially neutralize the positive impact of lower wage costs. In addition, some automotive suppliers have yet to realize the full expected cost advantages from procurement and production in low-wage countries. Only 11% of the respondents indicated that they were achieving a significant cost advantage (greater than 10%). Additional cost drivers related to globalization include qualification of employees, information technology, and custom duty, taxes and local conditions.

Figure 1: New Levers for Cost Savings



Source: Capgemini

Figure 2: The Cost-Management Matrix



Source: Capgemini

### How to Use the Levers to Achieve Savings

Supplier companies have tended to overlook these four levers, viewing them as being more difficult to control than the conventional cost categories. However, our analysis revealed that these levers offer automotive suppliers potential for significant cost reduction and should be in the forefront of cost-management efforts.

To understand the true value of these levers and how to use them for cost savings, the different cost drivers of each category have been represented in a matrix (see Figure 2) and classified according to their cost impact and “influenceability” – that is, the ability to influence the individual cost drivers. For example, a cost driver that is based inside a company might be influenced fairly easily, whereas a

cost driver arising from both external and internal circumstances might be influenced to some extent. In contrast, a cost driver that is subject entirely to external factors might not be influenced at all.

Consider the example of material costs: The market price for zinc is defined externally and cannot be influenced directly. Thus, the zinc portion of products can be reduced as an internal response to a steep increase in price. In contrast, the effectiveness of the procurement process can be completely influenced within a company. So, material costs for zinc can be reduced by bundling, global sourcing or renegotiating.

The research found differences in influenceability depending on the cost category. For example, cost

drivers arising from collaboration with customers can be influenced internally for the most part. However, many product requirements are specified by the customer or the relevant legislative bodies and can be influenced only to a certain degree.

The most important cost drivers are those that can be greatly influenced internally and, at the same time, have a high cost impact. The further to the top right-hand corner that a cost driver is located in the matrix, the more profitable its optimization will be. Of course, it is important to keep in mind that the cost impact of the different cost drivers can vary from company to company.

## Recommendations to Improve Cost Management

It became evident that the influenceability/cost impact relationship should be the basis for targeted and successful cost-cutting measures. The research – and, in particular, the matrix exercise – led us to a number of key conclusions and recommendations for automotive suppliers:

1. **Cost drivers rather than the type of costs should be the starting point for any cost-management initiative.** Conventional cost-cutting measures such as finance/controlling, purchasing/supplier, manufacturing and HR/administration are often ineffective beyond the short term, largely because they focus on the type of costs.
2. **Knowledge of the extent of influence for each cost driver is essential.** It is not enough just to consider the impact of the drivers on costs. In some cases, the cost driver may have a significant impact on cost, but can only be partially influenced.
3. **Employee qualification is a crucial issue.** The impact of employees on company performance and the potential for cost savings should not be underestimated or overlooked.
4. **The increasing complexity of products is a significant cost driver.** As product complexity can be influenced internally, this lever should be applied to reduce costs.
5. **International supply chains lead to high costs in logistics and IT.** Therefore compatible systems as well as transparent and predictable processes must be used to counteract costs.

6. **To avoid unnecessary costs, automotive suppliers should collaborate closely with suppliers and customers right from the start of an innovation process.** Cross-functional teams should be used to identify customer desires at an early stage to avoid negative investments and to reduce product development processes.



### About Capgemini

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More information is available at [www.capgemini.com](http://www.capgemini.com)

This summary of Capgemini's cost-management research provides a topline view of key findings from the study. Yet there is much more that can be explored and applied to your own organization. For additional information about our automotive supplier research or how we can help your company implement more targeted and effective cost-cutting measures, please contact:

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