Incentives and the Automotive Industry

Segments discussed in this paper:

Automobile Manufacturer to Consumer
Dealer to Consumer
Automobile Manufacturer to Dealer:
Sales Incentive Programs
Aftermarket
Agencies
Program Measurements
Conclusion
Research
Sources

About this paper:

Each automotive segment views incentives differently and has a unique distribution channel to consider. In this paper, we'll explore auto manufacturers use of incentives in various ways, including incentives targeting consumers and dealer sales forces, the aftermarket (parts sales) to their distributors and consumers, and how advertising agencies view incentives as a strategy to increase automotive client sales.

We'll look at the impact that discounting and traditional incentive and pricing strategies have had on the automotive business, and implications for the future.

Automobile Manufacturer to Consumer
-Purchase Incentive
-Gift After Purchase/Customer Loyalty
-Test Drive

Purchase Incentive

When the automobile industry announces incentives of up to $4000 per vehicle, we might assume that the “incentives” may be a mix of merchandise, travel and possibly cash used as a marketing strategy, and that they’re actually spending those dollars. You know what they say when we “assume”....

When an auto manufacturer says “incentives”, they mean cash. Cash back at time of purchase, finance incentives, lease pull-ahead or cash applied to the down payment. They do use merchandise and travel (as outlined below); however, “incentives” most often describes a discount and pricing strategy rather than a promotional marketing tool.
The discount or incentive amount per vehicle is a product of historical data, inventory levels, market elasticity of demand and product pricing. And although incentives must fall within target ranges dictated by the corporation and are technically budgeted, incentives are not a “spend” but rather a reduction of profit margin. The discussion of “value pricing” is simply making that “right price” calculation on the front end rather than adjusting the price with incentives later.

Whether to use cash incentives or to consider a non-cash promotion is determined by the goals at that time. Cash is used to move inventory and make price adjustments. Non-cash initiatives are used to “sweeten the deal” when cash incentives are no longer enough, or to launch a new vehicle without discounts. Strategic partnerships are often formed that bring the vehicle brand together with one of their advertising partners (magazine or interest group), to use a product to catch the attention of a different demographic group. For example, a vehicle brand with an older median age owner may use a new cool premium to catch the attention of a potential younger audience for the vehicle.

When you see the occasional non-cash program, very often there is an option to “cash out” rather than accept the promoted item (whether it’s merchandise, travel or a gift card). It’s less important that the customer actually redeem the premium – more important that they make the connection between the attributes of the premium/product and the attributes of the brand. If the customer needs the cash in order to make the down payment or to qualify for financing, that option is available to them.

Automobile manufacturers are convinced that cash is the most effective way to move vehicles. Regardless of the type of merchandise used, it will not appeal to 100% of the target audience. Cash has universal appeal, and the auto manufacturer knows exactly how much cash will provide a specific sales lift for a given demographic. The decision is then weighed whether to provide an incentive on the vehicle to sell through current vehicle inventory or production, or whether it’s more cost effective to cut back production, eliminating work shifts and possibly idling plants.

While auto manufacturers acknowledge that the consumer is now trained to wait for incentives before they buy, they still consider cash to be “fool-proof”. They believe that when (or if) they offer a merchandise item in place of cash, they run the risk of alienating consumers that are not moved by that particular item. Auto manufacturers firmly believe that “merchandise does not drive vehicle sales”.

Technological advances allow us to obtain more information than ever about the lifestyle, buying patterns, hobbies and interests of our customers and prospects. Developing a tangible incentive program that is likely to appeal to different market segments is entirely possible in today’s world.

Automotive experts predict that the current “employee pricing for everyone” programs will quickly evolve into a “value price” scenario. When that takes hold, automobile manufacturers will have difficulty providing significant cash incentives on the lower retail price. Of course, product quality, features and styling must be there, but vehicle brands will once again be looking for a way to communicate brand attributes and differentiate themselves.

Implications for the auto manufacturer include the realization that price promotions alone are a zero-sum game; short-term growth is obtained at the expense of future growth. Pricing has evolved as the major strategy to achieve short-term goals, however a price/value strategy would better
position auto manufacturers to achieve long-term profitability and market share. The automobile manufacturers that understand the connection between customer loyalty and increased profits will be looking for alternatives to cash incentives.

Gift After Purchase/Customer Loyalty efforts:

Contrary to the theory that says flat or declining sales periods are the perfect time to implement incentives or other marketing strategies, automobile manufacturers are most likely to employ non-cash incentives when market share is up and sales are good – in a non-risk environment, rather than when such a program would be most beneficial.

Because the current corporate climate is so focused on immediate results, a long-term customer loyalty effort is considered very risky and not essential to driving sales in the next quarter.

Automobile manufacturers have implemented customer appreciation or loyalty programs from time to time with very positive results. The following are post-program survey results from a gift-after-purchase program designed to surprise and delight the consumer:

- 75% of recipients told others about the gift
- 30% of those told 4 to 7 people
- 98% would recommend the brand to others
- 71% said the gift exceeded their expectations

Budget cuts inevitably derail these programs before the crucial piece of information that would validate the program can be gathered: re-purchase data. Management turnover, short-term focus on stock price and market share targets make it very difficult to maintain a long-term marketing or customer loyalty strategy.

Experts agree that building loyalty requires tracking what’s important, aligning incentives and rewarding the desired results, and making sure that the customers who provide or create the most value receive the most benefits.

Developing reliable loyalty measures would be much more effective in predicting re-purchase numbers than customer satisfaction surveys. Gift after purchase or other loyalty programs that continue long enough to track re-purchase data would provide the auto manufacturer (and dealer) with very valuable information for future planning and forecasting. (And what consumer wouldn’t rather receive a gift than yet another satisfaction survey...?)

The popularity of leasing vehicles has shortened the selling cycle amplifying the implications of customer loyalty on the bottom line. Research is beginning to prove that shareholder value comes from customer retention and loyalty. Loyal customers provide lower selling costs, increased profitability over time and will often pay a higher price for the product.

Test Drive

Test drive offers are used to get the customer into the dealership, but should also serve to qualify the customer and get them into the vehicle for demonstration. Typically, auto dealers are split between two schools of thought: those that believe “any traffic is good traffic” and those who believe that “only qualified prospects are valuable”.

Some test drive promotions are developed at the manufacturer level, others by individual dealers or dealer groups. Test drive programs are often proposed by the advertising agencies to leverage a media buy or to enhance a campaign.
A program based upon sharing a percentage of the sale price or profit margin and directly targeted to the consumer demographic rather than related to media issues should achieve the mix that the Dealer is looking for: The right offer that’s sufficient to bring in the target prospect, but not SO compelling that it brings in people who are not at all interested in the vehicle. Likewise, a strategic program that offers a test drive as well as a tangible purchase incentive would provide a complete program that would capture both trial and purchase data.

Funding such a program is tricky, as dealers and auto manufacturers continue to debate which one of them “owns” the customer: Is a vehicle owner a customer of the brand, or a customer of that particular car dealer that may also sell other brands?

Implications for the dealer: there is clear evidence that test drives equal sales. Targeted non-cash incentives should be used to attract the attention of the right qualified audience, and structured so that both test drive and purchase information is measured.

**Dealer to Consumer**

Individual dealers and dealer groups will frequently develop their own consumer incentives independent of national promotions that may be a mix of cash, merchandise, travel and gift certificates. Dealers are more entrepreneurial than the corporation, are more flexible, can put plans into action quickly and are typically willing to experiment with new program concepts.

Auto Dealers are very aggressive in developing programs to drive sales, and are willing to try new program concepts that have proven successful for other retailers. The manufacturer may be reluctant to fund a program without a proven track record, however, once the dealer-funded program is proven successful, the manufacturer may make the financial investment and adopt that same program for roll out on a national basis.

Auto Dealers understand that a loyal customer is a profitable customer. While a fair price for the vehicle is important, would a loyal customer pay a little more for a vehicle from a dealer that offers exceptional service and value: a dealer that drops off and picks up your car for service, schedules maintenance at your convenience, always provides a loaner, returns your car washed and vacuumed, pro-actively arranges for warranty work or to share the details of a lease pull-ahead program for which you would qualify? Would that dealer sell at a slightly lower price to a loyal customer who refers family, friends and neighbors to that dealership year after year?

**Automobile Manufacturers to Dealers: Sales Incentive Programs**

A wide variety of sales incentive programs are used to motivate the dealer sales force, and the corporation will frequently use performance improvement companies to design these programs. While they use a mix of cash, merchandise, travel and gift cards, suppliers for these programs are often selected contingent upon their ability to manage a large database of participants, promotional funds or rebates, allowances and other components.

Programs offered from the manufacturer to the dealer may involve audiences other than the sales force such as dealer principals, sales managers and service technicians. Offshoot programs aimed at financing, service targets, accessory packages and training components may also be in the mix.
Because profits from vehicle sales have been largely driven by cash incentives, these budgets are not based upon incremental sales or sales volume, but are fixed budgets. And, the objective is not always to increase sales – the company may be using travel programs as a way to reward their top dealers and give them face time with the corporate executives, or objectives may be tied to training and customer satisfaction index scores.

Once a program decision is made, the details must be communicated to thousands of independent dealers across the country, including all of the independent sales representatives. Because these programs require extensive administration it’s a challenge to show real value for the program budget.

While some of these programs involve cash awards, travel and merchandise provide more residual value.

Incentive Federation research \(^3\) shows that:

- Three of 5 respondents agree that a **cash payment is perceived to be part of an employee’s total remuneration package**.

- About 4 of 5 respondents (approx. 78%) perceive that **travel is remembered longer than cash**; about 4 of 5 (84%) agree that **merchandise is remembered longer than cash**. Nearly two-thirds of respondents (62%) feel that **cash is remembered for the shortest time**.

- Slightly more than half of the respondents (53%) agree that employees tend to look at bonus payments as something they are due as part of their compensation package.

Implications for the auto manufacturer: A Wall Street Journal analysis reveals that satisfied, happy employees have a significant impact on company profitability.\(^4\) Many companies mistakenly focus on capital productivity rather than employee productivity. Even slight changes in employee productivity can have a profound impact on shareholder returns.

In publications such as the New York Times, articles identify employee incentives as a motivational tool as a current trend, referencing companies such as Dell, Southwest Airlines and Starbucks that are employing People Performance Management with obvious success.\(^5\)

A results-based incentive program design (that includes employees beyond the sales force) would allow the manufacturer to drive and reward employee behavior in a way that will not be confused with compensation. Building ROI measurements into the program will ensure full value from the incentive program investment, and human resource management will become a core process rather than a support function for companies that understand this correlation.\(^6\)
Aftermarket – Parts sales to Dealers, Distributors, Installers & Consumers

Dealer Loaders
Pull-through promotions
Training Programs
Consumer Offers

Dealer Loaders

Parts are sold from the manufacturers through car dealers and warehouse distributors (WD's); both of which can purchase and sell competing brands. The manufacturer will offer incentives for the dealer/distributor to purchase parts (load in). In addition to discounts on specific products (also a means of adjusting product pricing), merchandise and travel programs are very popular.

Because dealers and distributors typically earn promotional funds or discounts based upon their purchase volume, they have funds available to run tangible incentive programs to help them move the parts back out to their customer base (pull-through).

Dealers and warehouse distributors have a wide range of education and experience; some are well-equipped to develop their own marketing and sales promotions, create their own graphics, etc.; others do not have the resources in-house to design or execute these promotions.

Parts manufacturers that provide the dealer/distributor with an easy-to-implement pull-through promotion in conjunction with a dealer loader will ensure that a consistent message is communicated, and will see the best results.

Pull-through Promotions – from the WD to Installer

These programs are designed to help the warehouse distributor move the parts back out of their warehouse, and are particularly successful when paired with a dealer loader.

Pull-through programs are directed at the installer who may have the choice of a number of parts brands when repairing a vehicle.

This audience likes to use their own product (buy 1 get 1 free), but does understand the value of promotional merchandise and non-cash incentives. The items must have universal appeal to their audience and offer value for the price. Because a low-cost item is often used, the challenge becomes identifying a compelling item that offers enough value to change buying behavior. Warehouse Distributors also understand and appreciate the residual value provided by promotional products. The WD frequently uses apparel and other promotional merchandise that pairs their name or logo with the parts brand logo. This reinforces the connection between the WD and the brand to the consumer, and also serves as an additional advertising vehicle.

Warehouse Distributors are often very familiar with their customer base and plan and execute their own loyalty programs. They know their customers on a personal basis, understand their interests and often plan events or activities that they know their customers will enjoy. Event marketing and frequent buyer programs are important and meaningful to this group.

Training Programs: Parts Manufacturer to Warehouse Distributor/Installer

Because many of the warehouse distributors, dealers and installers can sell competing brands, it’s certainly to the manufacturer’s benefit that the sales rep and technician are well versed on their products. The parts manufacturer looks for ways in which to encourage participation in training programs, which can include comparisons with competing parts brands, review product features and benefits, provide technical information and share best practices.
It is difficult for the parts manufacturer to require training, so incentives work very well as the motivation to complete training courses. Other methods to encourage service excellence and product knowledge include certification programs and technician competitions that recognize and reward excellence in this area. In addition to the program awards, results are well publicized by the parts manufacturer on a local level as well as nationally.

**Consumer Offers: Dealer to consumer**

The new car dealer is not required to purchase manufacturer parts. Dealer loader programs help to get the parts onto their shelves; national advertising and consumer promotions help to get them back off of the shelves. While the dealer is interested in providing vehicle maintenance and service to the consumer, the parts manufacturer is interested in making sure their branded part is used on the vehicle. This can be accomplished by providing an incentive for the consumer to ask for that brand.

Discounts and service offers (such as a free oil change) are used heavily here, but non-cash programs that offer a practical, useful item are also valuable. Programs coordinated with national advertising programs that drive the consumer to the dealer are especially effective.

**Implications for the Aftermarket: Non-cash incentives for this channel offer the opportunity for a fully-integrated program combining training with an on-going advertising message as well as an effective push/pull merchandising and sales strategy.**

**Agencies and Automotive Manufacturer Clients**

While advertising agencies may naturally become involved in promotional marketing in the course of providing their services to automotive clients, motivation and incentive program design may not be within an agency’s core competencies. The People Performance Management curriculum just being introduced in marketing schools will provide the formal training that advertising agency personnel (and marketing professionals) have not traditionally received. Agency employees learn from each other and reference what has historically been done, but may or may not follow accepted program design.

Advertising agencies are proactive in proposing concepts based upon their perception of the brand’s needs and will often back into the rule structure and goals accomplished. For example, an ad agency may propose a consumer or channel premium to leverage advertising spending, laying out for the client the benefits of that program rather than meeting assigned goals. In this case, the premium is seen as a “bonus” rather than a targeted strategy to achieve specific objectives.

Agencies perceive incentives or premiums as a way to connect an attitude with a brand (pairing a product with a new and exciting electronic item for example would encourage the consumer to view that product as “cool”).

Premiums are understood as something tangible and long lasting that support the advertising message. When sufficient time and consideration is taken to match the premium to the brand attributes, this can add strength and value to the advertising campaign. Premiums can also be used to show a “bump” in sales when other traditional programs have been running for some time.

Premiums are especially effective when the consumer is fanatical about the brand — anything with that logo on it becomes a collectible and a “must have” for customers loyal to that brand.
Advertising agencies perceive premiums or incentives as a nice “add-on” to a campaign, but acknowledge that when budgets are tight, this may be the first component to be eliminated by the client. While advertising agencies are in an excellent position to recommend premiums or incentives, these programs often compete with media spending and other core agency services. Direct Marketing or Promotion Agencies may have fewer conflicts and be more likely to recommend promotional marketing strategies.

Implications: An agency that fully understands the specific marketing goals of that brand and partners with an incentive professional to design a promotion to accomplish those goals will be providing the best recommendation to their client. Likewise, incorporating a customer loyalty component to campaigns or promotions will contribute to long-term shareholder value for their automotive client.

**Program Measurements:**

All segments attempt to measure program effectiveness, or at least target some program components, but a true Return on Investment (ROI) calculation is still rare (unless they’re working with an incentive professional or performance improvement company that provides this analysis). Lacking baseline data, and with a long history of running similar programs, few segments are willing to eliminate all programs for a period of time to “see what happens.”

Programs are still very much subjectively regarded as “successful” or “unsuccessful.” Whether program goals are achieved or not, results are attributed to the factor(s) that differed from the last program, however, scientific measures are typically not in place to verify these results.

The SITE Foundation and other incentive industry resources offer a number of measurement tools that provide the means to collect concrete data relating behavioral changes to achieving goals and profitability.

**Conclusion:**

Technology is facilitating targeted marketing, allowing auto manufacturers to differentiate by brand, by vehicle within a brand, and by market segment within the vehicle demographic. It is very possible to design and execute non-cash programs directed at a specific market segment.

For the first time, stock analysts are looking at motivation and its relationship to profitable and successful companies – research that automotive manufacturers have not yet internalized. The tools are available for the automotive industry to consistently use a statistical process to relate behavioral changes to goal achievement. The transition from a pricing strategy alone to a focus on and commitment to customer and employee satisfaction and loyalty will yield the greatest results for increasing sales, profits and long-term shareholder value.
Research:

A series of interviews was conducted with contacts in all segments of the automotive industry addressed in this paper. Information provided in this paper is taken from respondent’s answers to these questions:

Briefly describe the program:

1. What was the main program objective?
2. How were the goals or objectives determined?
3. Who was the specific audience for this initiative?
4. Number of participants:
   a. Did you have different performance levels?
   b. How was the rule structure developed?
   c. Did you involve the participants in program design?
5. How was the program communicated?
6. How did you determine the incentive to use?
7. How was the program budget developed?
   a. How was the award value determined?
   b. Fixed or variable budget?
8. What elements of the programs were measured?
9. How did you track and report participant progress?
10. What calculation did you use for Return on Investment?
    a. Results achieved vs. expected results: surprises?
    b. What other knowledge was gained from program reports?
Sources:


(3) A Study Conducted among Current Users of Merchandise and Travel Items for Motivation/Incentive Applications, prepared by the Center for Concept Development, Ltd, published by the Incentive Federation, Inc. May 2005

(4) “Happy Workers are the Best Workers”, by Steven Kent. Wall Street Journal, September 5, 2005.


(7) People Performance Management: business philosophy based on the theory that happy employees significantly boost profits. For more information on The Forum for People Performance Management, visit www.incentivecentral.org or www.performanceforum.org.