Report

Roland Berger

MIDDLE EAST

The future of automotive distribution in the Middle East

KEY IMPLICATIONS FOR
THE MIDDLE EAST MARKET

Roland Berger

MANAGEMENT SUMMARY

Automotive sector distribution is undergoing a transformative journey impacted by megatrends around new mobility concepts, autonomous driving, digitalization and electrification. This has resulted in several new business models being explored, with OEMs, distributors and new players, such as digital platforms and tech providers, looking to introduce highly digital and agile sales models.

In parallel, as the number of electric vehicles rises, diversification of the revenue pool and the relevance of value-added services will increase in the distribution business. Greater focus on the certified pre-owned (CPO) business and expansion of subscription sales should also help distributors maintain their relevance as car ownership becomes relatively less important for younger generations.

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1 / Introduction

Automotive distribution in the Middle East[1] is expected to evolve significantly in the coming years. The region witnesses 2–3 million light vehicle sales every year and is home to a ~35 million passenger car fleet.

Given the limited presence of local manufacturing activity, dealers and distributors have long been key partners for OEMs entering the region, taking more of a leading role in enabling sales compared with other markets. Local distributors, in fact, have invested heavily in building the local image of the brands while integrating throughout the sales and aftersales value chain.

Roland Berger's MADE framework outlines the four key trends that will shape the automotive industry of tomorrow: Mobility, Autonomous, Digitalization and Electrification. The infographics below illustrate how these trends are already transforming the regional landscape of vehicle sales and distribution activities in the Middle East. → A → B

While some regional players have already started integrating these trends in their strategies, we expect more such efforts in the coming years.

1) Middle East refers to the following countries: Bahrain, Egypt, Iran, Iraq, Israel, Jordan, Kuwait, Lebanon, Oman, Qatar, Saudi Arabia, Syria, United Arab Emirates and Yemen

A / "MADE trends" are defining key automotive distribution trends in the Middle East

Non-exhaustive

Key trends impacting automotive distribution	Associated "MADE" trend	Impact timeline
Customers increase their usage of digital channels for research and purchasing	d Increased digitalization leading to higher reliance of customers on digital channels	Short-mid term
Second-hand vehicle sales become more organized and new sales models are deployed	d Rise of multiple online players with varying business models for used car trade	Short-mid term
Drivers are less attached to vehicle ownership – subscription and usage models become more widespread	m Increase in preference for shared mobility over vehicle ownership	Short-mid term
Electric vehicles are more prevalent and transform the automotive distribution business	e Increasing penetration of electric vehicles, impacting vehicle sales models and aftersales business	Mid-long term
Dealers increase their offerings of value-added services	m e Electrification and mobility driving advanced services such as battery/charging or smart mobility solutions	Mid-long term

Overview of MADE trends: m New Mobility; a Autonomous Driving; d Digitalization; e Electrification

B / Overview of the potential business impact of key trends – Way forward for distributors and dealers

Key automotive distribution trends	Impact on revenues for distributors/dealers	Impact on CAPEX/OPEX for distributors/dealers
Rise in the usage of digital channels by customers	No major impact	Set-up costs for online channel
Formalization of used car channels and innovation in business models	Potential rise in used car sales activity	Increase in CAPEX as well as associated OPEX for used vehicle business
Evolution in the car ownership trends – rise of subscription/other models	Distribution of revenue realization over longer term	? Dependent on whether OEM offers subscription benefits to dealers
Rise in vehicle electrification	Potential decline in aftersales revenue	Decrease in aftersales arm's operating costs – CAPEX for workshops
Increase in offerings for value-added services	Rise in one-time/ recurring revenue	Increase in associated operating costs for value-added services

Potential way forward – To be evaluated (case by case)

Enhance focus on non-traditional sources of revenue

Diversify into other profitable automotive/ adjacent businesses

1) CAPEX: Capital expenditure; OPEX: Operating expenditure
Source: expert input, Roland Berger

Impact | Increase | No/limited impact | Decrease

2 / Buying a car in the Middle East in the era of digital everything

The digitalization of all aspects of our life and the unstoppable technological advancements find a perfect match in Middle East consumers, where two-thirds of the current population is aged 35 or under and Internet penetration has reached ~96% in key markets (such as the UAE and Saudi Arabia).

Buying a car is no exception – according to data, 96% of prospective auto buyers in the UAE and Saudi Arabia initiate their purchase journey online, leveraging the Internet to research and explore their new car. → C

Up to two-thirds of this research is conducted on mobile devices such as smartphones and tablets. Once they find their perfect car, over 50% of customers would also use the Internet to signal their interest and get quotes, continuing their all-digital experience.

In many cases, the very first time customers approach dealerships and transfer their journey to the real world is at the moment of finally closing the purchase of their vehicle. Moreover, even there, customers use their smartphones to support their physical shopping experience with details on configuration, finance package, accessories and services.

C / Digitalization statistics from Roland Berger's Automotive Disruption Radar, June 2022

Usage of Internet in vehicle purchasing – To what extent will you use the Internet? (average % of people who selected the usage)

	... to inform me about the car itself, its features, etc.	... to get offers to buy	... to buy directly on the Internet
Bahrain	85	55	15
Kuwait	85	45	15
Oman	80	35	10
Qatar	80	50	20
Saudi Arabia	80	50	15
UAE	80	50	15
China	90	80	30
Europe [1]	75	53	16
United States	75	40	20
Global average	78	52	16

1) Average score for Belgium, France, Germany, Italy, Netherlands, Norway, Spain, Sweden, UK
Source: RB online survey September 2022: 22,704 participants – Participants by country: Bahrain (152); Belgium (976); Brazil (1,002); Canada (999); China (987); France (977); Germany (999); India (998); Indonesia (1,013); Israel (984); Italy (975); Japan (1,000); Kuwait (300); Netherlands (988); Norway (964); Oman (200); Qatar (300); Saudi Arabia (1,000); Singapore (961); South Korea (996); Spain (978); Sweden (978); Thailand (1,000); UAE (993); UK (1,001); USA (983)

To accommodate this evolution and the increasing consumer preference for digital sales, Middle East distributors, dealers and OEMs are revamping their platforms and digital ecosystem to include ever more services and enhance the buyer experience. → D

While the direct online purchase of cars in the Middle East is not fully developed, almost all OEMs/NSCs (National Sales Companies) have started to progress toward the implementation of an omnichannel journey. This channel strategy combines physical experience with advanced digital services and platforms for enhanced consumer interaction. Digitalization does not stop at the point of purchase, with aftersales and trade-ins being digitalized as well. Immediacy and superior experience are among the main reasons why online channels have become so popular.

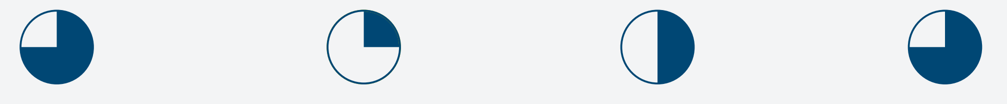
The transition to the digital channel generates significant amounts of customer data that can be leveraged for advanced product, service and channel offerings. Given the increasing relevance of data-driven business decisions, OEMs are incorporating standard practices throughout their sales network in order to control the data.

However, certain customers cite price transparency as one of the key barriers to finalizing their purchase online, as they fear they could get a better deal at the dealership. Also, as human interactions are not fully replicable online, dealers should aim to become an experience center, bringing customers closer to the brand/vehicle in the offline touchpoint(s) of their journey. This can be done through a variety of formats that favor client convenience and proximity at each step, such as pop-up and urban stores.

Non-exhaustive

D / Digitalization of the automotive purchase journey in the Middle East

	Customer research and awareness	Purchase (new car)	Aftersales	Trade-in/ used car sales
Key activities	• *Pre-landing activity (advertising ...)* • Vehicle browsing • *Vehicle configuration* • *Financing exploration* • *Offer/lead management* • Test drive	• Vehicle purchase • *Configuration* • Contract signature • Legal and admin (registration) • Payment • Added services • Warranty extension • *Financing*	• *Service reminder* • *Service booking* • Service agreement • *Purchase of parts* • Repair status tracking and follow-up • Payment	• *Listing* • *Offer/lead management* • Purchase • Trade-in
Digitalization level				



Activities with current high degree of digitalization
Digitalization level Low → High
Source: Roland Berger

3/ Formalization of used car channels and innovations in the business models

The Middle East (ME) market witnesses a higher relative level of used car transactions every year. A total of 800k+ used cars were sold in the UAE in 2019, implying a 3.5:1 ratio of used to new car sales in the country. The used car sales trends are expected to stay strong in the coming years, with the sale of over 1 million used cars anticipated annually in the UAE by 2025, for example.

The ME market currently has three major categories of players in the used car segment. Along with the independent used car dealers and franchise-based dealers, there has been an increasing proliferation of online-focused players with varying business models. Some of these business models include classified/listing, marketplace and online auction-based sales.

There is a concerted effort from the used car players to create a seamless used car journey, offering attractive and easy-to-access financing options as well as value-added services such as doorstep test drive and delivery options. To increase consumer confidence around second-hand vehicles, the majority of them have started to offer detailed certification reports, coupled with extended aftersales and warranty packages. → E

A fundamental shift is expected in the used car market structure going forward. Historically, consumers in the Middle East exhibited strong preferences for C2C (customer-to-customer, peer-to-peer) channels for used car sales. However, these are expected to decline with the anticipated increase in customer confidence in the organized segment led by the independent and franchise dealers.

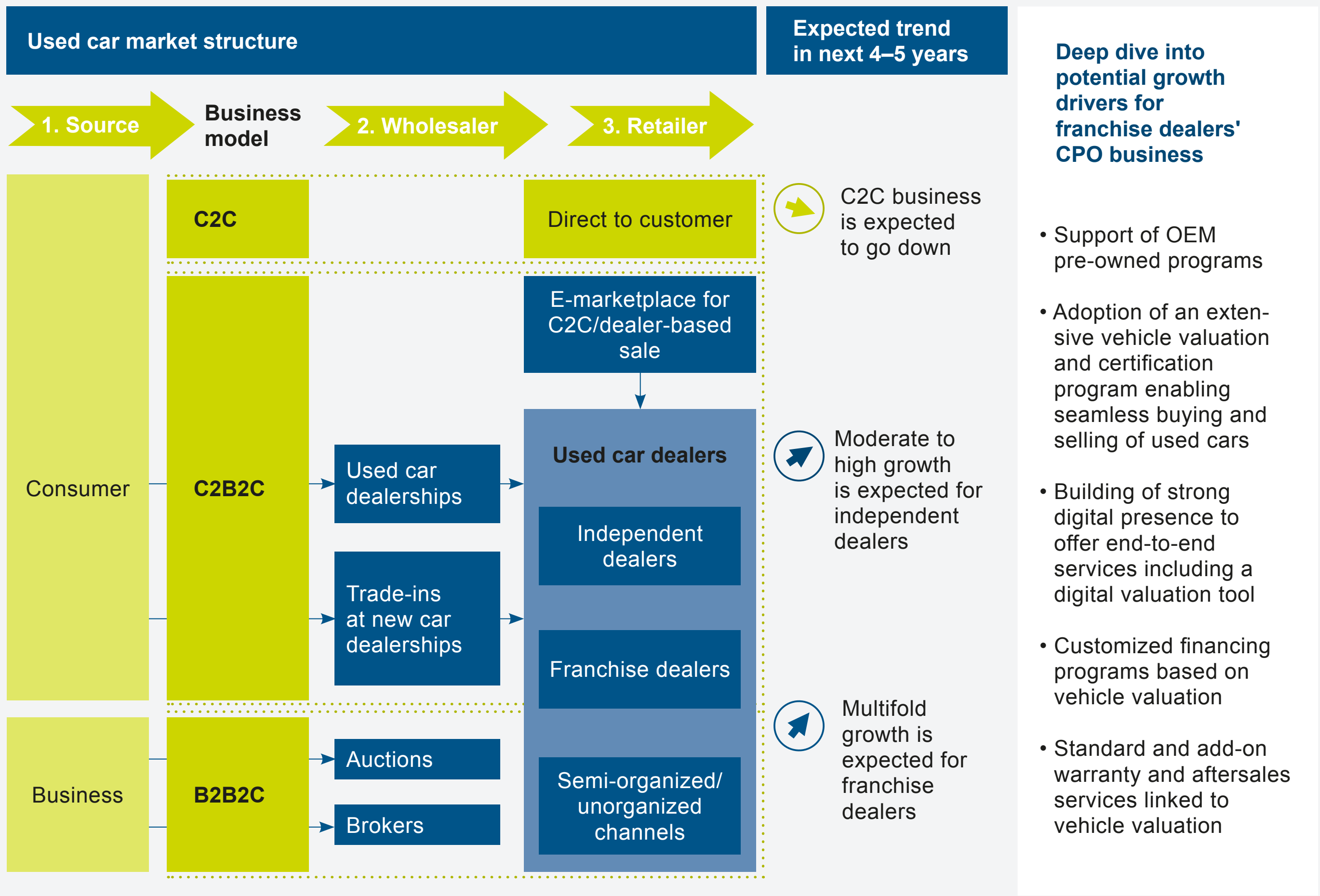
E / Current landscape of used car operations in the Middle East: Case study for the UAE

Categories of used car operators in the market	Online-focused platforms operating across various business models (e.g. classified, marketplace, online auctions)	Independent used car dealers (mostly part of traditional automotive business groups)	Franchised dealers with used car business presence
	• SellAnyCar.com • Carnab • CarSwitch • Dubizzle Cars	• Copart • Al-Futtaim Motors • Sun City Motors	• Premier Motors • AGMC • Abu Dhabi Motors

Snapshot of measures taken by the used car players – case study for Carnab	Money back guarantee	One-year warranty	Delivered to your doorstep	Multiple financing options
	A 10-day return policy on any car purchases through Carnab	Drive your car for one year with the peace of mind of a new car. You can even choose to extend it by another year	Simple viewings at your home or at any of our national branches	Hassle-free and quick financing made possible

Source: online channels, dealers' websites, Roland Berger

F / Used car market structure and expected shift: Case study for UAE



Source: expert input, Roland Berger

The penetration of strong, dedicated certified pre-owned (CPO) programs among the leading new car dealers in the UAE is currently 60%–70%. The used car business presents a strong opportunity to franchise dealers to diversify their revenue sources. Hence, we expect used car sales from franchise dealers to witness the strongest growth in the coming years (3x–4x sales in the UAE).

It will be important for automotive dealerships to seek OEM support and launch interactive digital platforms for their CPO business. An omnichannel retail strategy is expected to be the key to ensuring rapid ramp-up of the used car business. Such platforms will also offer data-driven insights to enrich the dealers' customer offerings. As the market evolves, we expect new business models around subscription and leasing to gain prominence for used cars as well. → **F**

The greater penetration of digital platforms increases the footprint and visibility of used cars across the region and beyond. Dealers may leverage such platforms and a coherent export/logistics infrastructure to offer their used vehicles in markets such as Yemen or some African countries.

The transition to EVs also opens up new opportunities for used car sales – more price-sensitive customers will tap into the used car market to access EVs with lower financial commitment. The residual values of EVs and their success in the second-hand market is still uncertain, as EVs are currently depreciating faster than ICEs due do quicker obsolescence.

In turn, opportunities may arise for dealers to drive the transition to electric through special offers and control of remarketing for used EVs.

4/ Subscriptions for the automotive industry

The overall shift in consumer preferences toward the shared economy and the associated models of ownership have impacted how people relate to their vehicle and the value they associate with owning one. Notably, younger generations are shifting toward more flexible solutions characterized by low capital commitment. In fact, 65% of people surveyed globally in our ADR study are already very familiar with new mobility concepts, such as car sharing and ride hailing.

In such models, customers subscribe to the service by paying a monthly/yearly fee for which they get to drive the car with all expenses included (except for gas). Subscription plans come with flexible tenures, typically ranging from one month to 48 months. The customer has the flexibility to upgrade the vehicle and associated services at some point during the contract.

While Europe remains one of the leading markets by revenues for such services, with Geely's new brand (Lynk and Co) having opted for subscription as their go-to-

G / Overview of key operating models across the subscription playbook in the Middle East

	1. Pure-play subscription platform	2. Brokerage subscription platform	3. Rental companies	4. OEMs
Operating model	Subscription of vehicles – Platform manages own stock	Subscription of vehicles – platform acts as broker for dealers (no own assets or fleet management)	Subscription as an additional service offering	Subscription as a financing option for OEM vehicles
Strengths	• Subscription business as core activity • Full margin control • Full customer journey awareness and management	• Leverage network and client base • High control over vehicle sourcing and life cycle	• Leverage network and client base • High control over vehicle sourcing and life cycle	• Leverage existing client base of dealer network • End-to-end control over pricing and margin • Control of the vehicle lifecycle
Weaknesses	• Balance sheet risk and fleet management • Brand establishment required	• Limited price power and margin control • Limited control over dealer-managed processes	• Cannibalization of existing rental and mobility business	• Cannibalization of existing sales and leasing channels • Potential conflicts of interest with dealer network
Examples (Middle East)	• MOOV by Al-Futtaim • Swapp	• Invygo • Carasti	• Selfdrive.ae	• Yet to be deployed in the Middle East

Source: Roland Berger

market model for the region, the demand for such services is also expanding in the Middle East (especially in the GCC).

We see three major types of benefits driving the customer appeal of subscription models:

A. The simplified digital experience offered by subscription platforms, enabling an all-digital purchase journey

B. Lower ownership risk manifested in lower capital commitment and an absence of residual value risks

C. Greater flexibility to upgrade vehicles and change ownership patterns

The quest for a profitable business model associated with subscription often relies on the ability to effectively manage the purchase price of the fleets.

MOOV is the most relevant case study for the Middle East. The platform is owned by a long-time Toyota distributor in the UAE (Al-Futtaim) and offers subscriptions as short as one month on the vehicles for which the company is an official distributor. Al-Futtaim's move sets a precedent for the region and proves the potential advantage dealers may have in such an ecosystem. → G

Distributors and dealers with existing large fleet sales could be able to secure lower purchasing prices from OEMs and insurance providers, while leveraging their fleet management and end-of-life management capabilities, in order to drive profitability. However, this will entail managing the risks associated with working capital, residual value and overall asset ownership by the entity managing the service.

OEMs are also adapting to the evolution in consumer preferences by intensifying their focus on B2B and fleet sales and developing tailored products for the segment. Vehicles dedicated to subscription and fleet sales are offered with more standardized specifications and finishing. Some OEMs have also launched their own proprietary subscription service, such as Porsche and Volvo.

In addition to this, OEMs are now offering specialized vehicle features as part of a monthly or yearly package (such as Tesla offering its Autopilot function on subscription), transforming certain optional extras into an on-demand function that can generate additional revenue. This could also imply limited upselling opportunity for distributors where OEMs are selling these services direct to customers as subscriptions.

5/ Rise in vehicle electrification and implications for car dealers

Electrification is currently a key automotive disruptor across markets, with some of the markets, such as Norway, significantly leading the electrification curve (>70% xEV penetration in 2021). By 2040, we expect 40%–50% of global new light vehicle sales to be electric. In the Middle East, we expect Saudia Arabia (KSA) and the UAE to also observe a significant rise in battery electric vehicle (BEV) penetration in the coming years. For KSA and the UAE, 40%–75% BEV penetration in new car sales is anticipated by 2035. → H

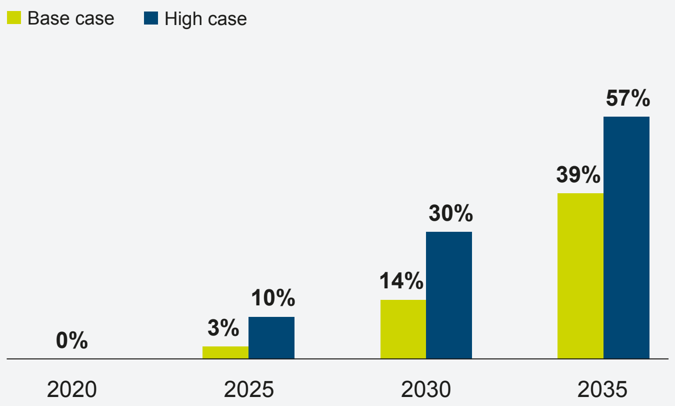
Regulatory push in both countries will be key to driving demand. While a certain level of penetration may be reached on the basis of OEMs' EV offerings and the consumer pull effect, a much higher penetration can be achieved with regulatory push such as emission restrictions and ICE phase-out.

Although Saudi Arabia currently has <1% EV sales, the upcoming local manufacturing by two EV-only brands (Lucid and Ceer), charging infrastructure set-up and increasing customer awareness are expected to drive EV sales in the medium to long term. High EV penetration is a core focus for Saudia Arabia, considering the electrification and sustainability goals of the Saudi Arabia's Vision 2030. The UAE witnessed ~3k BEV sales in 2021 (~2% penetration), with Tesla capturing ~60% market share. Going forward, we expect a steep rise in EV penetration. → H

The UAE's electrification growth will be led by its expanding EV charging network (300+ charging stations installed currently), availability of new EV models and sustainability targets.

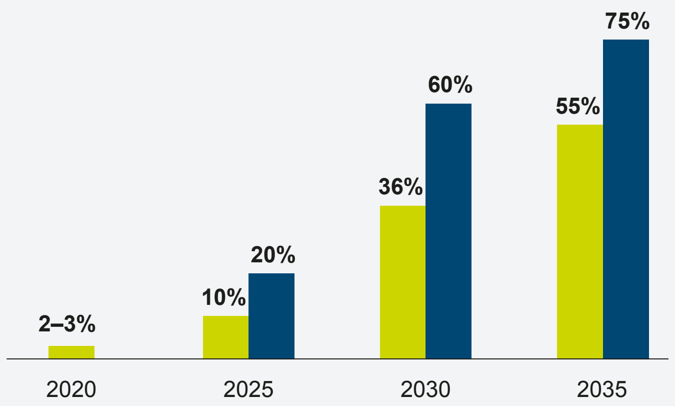
H / EV penetration scenarios in the Middle East: Case study for KSA and the UAE

EV penetration scenarios in Saudi Arabia, 2020–2035 [% of new light vehicle sales]



Electrification in KSA
Some of the key considerations and enablers that are expected to drive the adoption of electric vehicles in KSA will be local availability of EV vehicles, as well as deployment of EV charging infrastructure. Consumers in KSA will also need to be educated about EVs in order to increase their awarensss and willingness to embrace the transition to electric powertrains.

EV penetration scenarios in the UAE, 2020–2035 [% of new light vehicle sales]



Electrification in the UAE
In the UAE, public entities are actively involved in driving the growth of EV solutions in the country. Emirates such as Dubai have announced programs for swapping taxi fleets for electric and hydrogen vehicles as well as setting up 300+ charging stations. Government organizations in Dubai will also increase the number of electric and hybrid vehicles procured to 30% of the fleet in 2030. Such efforts are part of the UAE's roadmap to achieve net-zero emissions by 2050.

Source: expert input, Roland Berger

We expect two major electrification-related impacts to affect distributors and dealers in the Middle East region:

1. Impact of direct sales approach by new-age EV OEMs:
Most of the new-age EV OEMs such as Tesla, Nio and Polestar are adopting direct sales to maximize their value chain control. This could pose a threat to the distributors and dealers in the region. However, we expect most EV OEMs to collaborate with distributors/dealers in order to maximize penetration in the region and conduct efficient operations.

2. Impact of changes in aftersales business:
Electric vehicles require significantly less maintenance than internal-combustion engine (ICE) vehicles. While EVs don't require engine-related servicing, even brake pad changes are limited due to the extended part life. In general, EVs are expected to require ~50% less aftersales than their ICE counterparts. Besides the revenue shrinkage, EV maintenance may require dealers to install specific workshop machineries suited to the technology. More qualified technicians are required to cater to battery, electric motor and electronics-related requirements. → I

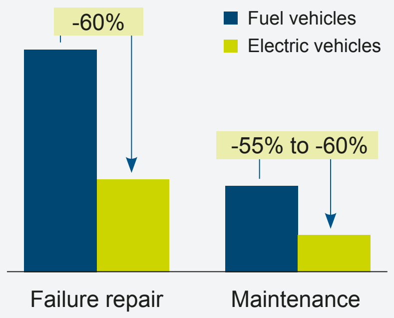
I / Impact of electrification on the Middle East aftermarket

Car parc

Total **vehicle parc is not expected to increase** through the introduction of EVs, as there will instead be a **substitution of traditional vehicles**

Aftersales

Service revenues and car maintenance needs of electric vehicles are almost **50% less** than those of fuel-based cars



The powertrain of electric vehicles is less complex than traditional combustion vehicles, and distributes power differently, lowering the need for maintenance:

A. **Brakes:** Typical brake pad life is extended from 20,000 to 40,000 miles on ICE vehicles to more than 100,000 miles with EVs

B. **Oil changes and other engine maintenance:** EVs never need oil changes or ICE-related maintenance

C. **Parts:** An EV drivetrain has fewer than 1/10th of the moving parts of most ICE vehicles, leading to fewer part replacement requirements

Source: expert input, Roland Berger

6/ Increasing significance of value-added services

In the era of electrification and shared mobility, car dealers are increasingly focusing on alternate sources of revenue through various value-added services. Below are some of the services that are expected to gain more focus in the coming years.

A. EV battery and charging solutions:
Battery leasing and EV charging are expected to be the key services offered by dealerships to their EV customers. Battery leasing and battery swapping solutions can be offered by dealers in collaboration with the EV OEMs.

B. Connectivity and smart mobility solutions:
As connected vehicles become more common, distributors and dealers expand their offerings related to digital apps and solutions. Their portfolio may include digital services such as driver monitoring (e.g. for younger drivers), predictive maintenance, digital fleet management, concierge services, infotainment, roadside assistance and SOS services. These solutions can typically be priced with a fixed-plus-variable model and may be offered to both B2C and B2B/fleet customers.

C. Financial services:
Dealers may also want to look at new financial service offerings to enhance their revenue pool. This could include full-service leasing services in collaboration with financial institutions to offer tailor-made products to the customers. In the Middle East, the B2C segment of leasing seems currently underexploited: dealers may develop full-service leasing models with a mono-brand or multi-brand offering, leveraging their used car inventory.

7/ FINAL CONSIDERATIONS

The trends described in this publication are expected to have a multifold impact on the business of dealers and distributors in the Middle East, both in terms of their financial performance and the evolution of their product/service portfolio.

Most of the trends linked to mobility and electrification entail a declining share of the pie for the distributors and dealers unless concerted efforts are made to diversify into new products and adopt new business models.

To ensure revenue flows and profitability, dealers and distributors should intensify their focus on non-traditional sources of revenue (such as value-added services, subscription/leasing formats and used car platforms) and could consider diversifying into other businesses, either organically or inorganically. Based on the emerging automotive ecosystem in KSA and other markets, opportunities could be found in EV/component manufacturing, mobility services, battery recycling/repurposing and other emerging areas. → J

Investments and M&A activity will be required in the short/medium term to diversify into new products and adopt new business models. Dealers and distributors should prioritize the value chain segments in which they want to play based on the market potential and the synergies that exist with their current resources.

J / Overview of key trends and their impact on automotive distribution

Key automotive trends	Impact on revenues for distributors/dealers	Impact on CAPEX/OPEX for distributors/dealers	Impact on steady-state profitability	Timeline of the trend
Rise in the usage of digital channels by customers	No major impact	Set-up costs for online channel – costs may optimize with physical store reduction	Less operating costs for digital stores	Short-mid term
Formalization of used car channels and innovation in business models	Potential rise in used car sales activity	Increase in CAPEX as well as associated OPEX for the used vehicle business	Higher margin from used car business compared to new cars	Short-mid term
Evolution in the car ownership trends – rise of subscription/ other models	Distribution of revenue realization over longer term	Dependent on whether the OEM offers subscription benefits to dealers	Rise in margin from financing and aftersales packages	Short-mid term
Rise in vehicle electrification	Potential decline in aftersales revenue	Decrease in aftersales arm's operating costs – some CAPEX needed to upgrade workshops	Decline in high profit yielding aftersales income	Mid-long term
Increase in offerings for value-added services	Rise in one-time/ recurring revenue	Increase in the associated operating costs for value-added services	Relatively higher margins from value-added services	Mid-long term

Source: expert input, Roland Berger

Impact | Increase | Neutral impact | Decrease

AUTHORS

SANTIAGO CASTILLO

Senior Partner +971 56 656-9155 santiago.castillo@rolandberger.com

ARVIND CJ

Partner +971 54 581-0862 arvind.cj@rolandberger.com

SMRITI PRIYA

Senior Project Manager +971 50 172-6215 smriti.priya@rolandberger.com

ANDREA CAVALLERI

Senior Consultant +971 50 712-7615 andrea.cavalleri@rolandberger.com

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ROLAND BERGER GmbH
Sederanger 1
80538 Munich
Germany
+49 89 9230-0

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