Case Study: Strategies & Insights from Scania AB – Combating & Managing Industry & Global Economic Slowdown Effectively

“Management’s job is not to prevent risk but to build the capability to recover when failure occurs”
Case Study

Strategies & Insights from a Niche European Truck-Maker - Scania AB - Combating & Managing the Industry & Global Economic Slowdown Effectively

Introduction

The recent global economic slowdown had been the worst ever crisis to have hit the global economy since the Great Depression of 1930’s. Triggered by the financial system crash in the US first & followed by Europe during autumn 2008 the crisis caused dramatic deceleration in the global economic growth thereon. Almost all the industries & markets, especially in the western hemisphere, were significantly affected & impacted by the downturn.

The European market for trucks was no exception to the power of the crisis which had global dimension, impact & ramifications The Western European market for trucks almost halved in terms of demand in the year 2009 plummeting to 168,000 vehicles in 2009 as against 330,000 vehicles in 2008. The North American market too went through the carnage as the demand for class-8 truck sales in North America declined to 1991 levels.

Almost all truck-makers bore the brunt of the uncalled for crisis & deployed an array of coping strategies to best adapt to the rapidly altered market & industry dynamics as well as environment and thus went through a major transformation in terms of structure, alignment and stance while navigating through the unprecedented times.

This case study focuses on the niche European truck-maker; Scania AB, based out of Sweden, and provides insights into how it combated & managed to navigate effectively through the depths of the crisis by leveraging inherent structural strengths while simultaneously deploying & utilizing an array of strategies to ensure that Scania maintained its profitability track-record, unbroken for last 5 decades, on a year-on-year basis once again in 2009.

About the Company

Scania Aktiebolag (publ), commonly referred to as Scania AB or just Scania, is a global automotive industry manufacturer of commercial vehicles - specifically heavy trucks and buses. It also manufactures diesel engines for motive power of heavy vehicles, marine, and general industrial applications.
Founded in 1891 in Södertälje, Sweden, the company's head office is still in the city. Today, Scania has ten production facilities in Sweden, France, Netherlands, Argentina, Brazil, Poland, and Russia. In addition, there are assembly plants in ten countries in Africa, Asia and Europe. Scania's sales and service organisation and finance companies are worldwide. In 2009, the company employed approximately 32,330 people around the world as against 34,777 employees in 2008.

Scania is now majority owned by Volkswagen Aktiengesellschaft (more usually known as Volkswagen AG), the parent company of the German automotive concern, Volkswagen Group, making it the ninth marque of the Group.

Scania's logo shows a Griffin, from the coat of arms of the Swedish region of Scania.

Origins

Scania AB (Scania is Latin for the province of Skåne) emerged from a merger between the two companies; Vabis and Scania. Further, Scania is the name of the southernmost non-administrative province in Sweden.

Vabis (Vagnsfabriksaktiebolaget i Södertälje) was founded in 1891 as a subsidiary of Södertälje based steel company Surahammars Bruk, manufacturing railway carriages. In 1902, engineer Gustaf Erikson designed the company's first truck, powered by a petrol engine and two-speed gearbox. A year later, the first order was placed for a Vabis commercial vehicle. By 1907, the company had developed a 3-ton truck, however, though it won a Swedish Royal Automobile Club award in 1909, the new range was a financial disaster for the company, failing to attract more than a handful of orders.

Maskinfabriks-aktiebolaget Scania was founded in 1900 in Malmö in the south of Sweden, and was in the beginning a manufacturer of bicycles, but by 1903 the first cars left the factory. Two years later, Scania built their first truck.

Following the financial problems at Vabis, the companies subsequently merged in 1911, creating AB Scania-Vabis. Engine and car production was moved to Södertälje, and truck production took place in Malmö.
Early Years & Growth Trajectory

World War I and 1920s

For the next few years the company's profits stagnated, with around a third of their orders coming from abroad. The outbreak of World War I, however, changed the company, with almost all output being diverted to the Swedish Army. By 1916, Scania-Vabis was making enough profit to invest in redeveloping both of their production facilities.

Following the war, in 1919, Scania decided to focus completely on building trucks, abandoning other outputs including cars and buses. However, they were hurt by the swamping of the market with decommissioned military vehicles from the war, and by 1921 the company was bankrupt.

After some economic difficulties in 1921, new capital came from Stockholms Enskilda Bank owned by the Wallenberg family, and Scania-Vabis became a solid and technically, high standing, company.

1930s and 1940s

During World War II Scania produced a variety of military vehicles for the Swedish Army, including Stridsvagn m/41 light tanks produced under license.

1950s and 1960s

During the 1950s, the company expanded its operations into new customer segments, becoming agents for the Willys Jeep and the Volkswagen Beetle, the latter being very profitable for Scania-Vabis. It also started to become a genuine competitor to Volvo with their new Regent truck which was introduced in 1954.

During this period, Scania-Vabis was to expand its dealer network, and country-wide specialist workshop facilities. By the end of the '50s, their market-share in Sweden was between 40 to 50%, and was achieving 70% in the heaviest truck sector - helped by the entrepreneurial efforts of their dealers into the haulier market.

Probably their largest impact was in export markets. Before 1950, exports accounted for only 10 percent of production output, but a decade later, exports were at almost 50% of output. Beers in the Netherlands became a very important partner. Beers became official importers for Scania-Vabis in the Netherlands, and established a dealer network, along with training programmes for both mechanics and drivers. Beers also offered free twice-yearly overhauls
of their customer’s vehicles, and offered a mobile service throughout the Netherlands with their custom-equipped service trucks. Due to Beers concerted efforts, Scania-Vabis market share in the country remained at a consistent 20% throughout this period. Scania-Vabis were to adopt the business model of Beers in their own overseas sales operations.

The 1960s saw Scania-Vabis expanding its production operations into overseas locations. Until now, all Scania-Vabis production had been carried out solely at Södertälje, but the ’60s saw the need to expand production overseas. Brazil was becoming a notable market for heavy trucks, and was also dependent on inter-urban buses, with particular requirement for the mountainous roads of Brazil which became night-on impassable at times. Scania-Vabis established its first production plant outside Södertälje, by building a new facility at São Bernardo do Campo in Brazil, which was completed in 1962, and this was to set the standard for Scania-Vabis international operations.

Closer to home, the recently formed European Economic Community (EEC) offered further opportunities. Based on their now strong presence in the Dutch markets, Scania-Vabis constructed a new plant in Zwolle, which was completed in 1964. This new Dutch facility provided Scania-Vabis with a stepping stone into the other five EEC countries, particularly the German and French markets.

In 1966, Scania-Vabis acquired ownership of a then valuable competitor - Be-Ge Karosserifabrik, who were based in Oskarshamn. Be-Ge had been making truck cabs since 1946, and had been supplying cabs not only to Scania-Vabis, but also to their Swedish competitors Volvo. It was normal practice for truck manufacturers to outsource production of cabs to independent bodybuilders, so their acquisition by Scania-Vabis seemed a good move. Be-Ge owner Bror Göthe Persson had also established an additional cab factory at Meppel.

Scania-Vabis continued their expansion of production facilities through acquisitions. In 1967, they acquired Katrineholm based coachwork company Svenska Karosseri Verkstäderna, and created a new subsidiary, Scania-Bussar. A year later, all bus production, along with R&D was moved to Katrineholm. Further production locations were added at Sibbhult and Falun, and Scania’s employee numbers rose, particularly at Södertälje.
Spate of Mergers, Demergers & Foiled Takeover Bids

Saab-Scania AB Merger

In 1969, Scania-VABIS merged with SAAB, and formed Saab-Scania AB. When Saab-Scania was split in 1995, the name of the truck and bus division changed simply to the present Scania AB. One year later, Scania AB was introduced on the stock exchange, which resulted in a minor change of name to Scania AB.

Thwarted Volvo takeover bid

On 7 August 1999, Volvo announced it had agreed to acquire a majority share in Scania. Volvo was to buy the 49.3% stake in Scania that was owned by Investor AB, Scania’s then main shareholder. The acquisition, for $7.5 billion (60.7 billion SEK), would have created the world’s second-largest manufacturer of heavy trucks, behind DaimlerChrysler. The cash for the deal came from Volvo selling its car division to Ford Motor Company in January 1999, but the deal had yet to be approved by the European Union.

The deal eventually failed, after the European Union disapproved the bid, citing monopoly restrictive laws as the merger would have created a company with almost 100% market share in the Nordic markets.

Foiled MAN takeover attempt

In September 2006, the German truck-maker MAN AG launched a €10.3bn hostile offer to acquire Scania AB. MAN AG later dropped its hostile offer, but in January 2008, MAN increased their voting rights in Scania up to 17%.

Scania as of 2010 – Snapshot

Headquartered: Södertälje, Sweden

Revenues: SEK 62 billion (Euro 6 billion approx.) in 2009

Business Segments

• Trucks
• Buses
• Engines
- Service related Products
- Used Vehicles
- Financial Services

**Employees:** 32,330 as of 2009 end.

**Market Capitalization:** EUR 2.252 Billion

**Key Competitors:** Volvo, Daimler, MAN, DAF

**Current Ownership**

As of December 31, 2009, the German automotive company Volkswagen AG is Scania's biggest shareholder, with a 70.94% voting stake (equity). It gained this by first buying Volvo's stake in 2000, after the latter's aborted takeover attempt, increasing it to 36.4% in the first quarter 2007, and then buying the remainder from Investor AB in March 2008. The deal was approved by regulatory bodies in July 2008. Fellow German truck manufacturer MAN SE holds a 17.37% voting stake in Scania.

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**Scania & the Downturn in the European Truck Market**

"It is the biggest market subsidence I have seen during my years at Scania, with a 50 percent drop in volume and a 60-70 percent decline in production during the first half of 2009," said Leif Östling, President and CEO of Scania.
He admitted to having been taken by surprise by the impact of the downturn, despite having experienced a number of economic downturns and both oil and dotcom crises during his nearly 40 years at Scania.

“This time the cyclical downturn for investment goods that comes at 7-8 year intervals coincided with a financial market collapse, which made the downturn extra powerful.”

The company, however, replied to & managed the situation reasonably well; by focussing on the three C's – Customers, Costs and Cash Flow while simultaneously leveraging the inherent strengths.

**Leveraging Structural Strengths & Nimble Strategic Management**

**Modular Product System – Product Customization along-with Commonality of Scale Advantages**

Scania has followed a modular product system since 1950’s and it has been a major factor behind the success of the company across markets as it enables the company to customize the products as per the customer specifications in addition to enjoying cost-savings originating from economies of scale. Modularisation in layman's parlance means that every customer is offered a custom-made vehicle at the optimum time. Since each vehicle is made entirely on the basis of an assessment of the customer's business need and the prevailing real-world situation, it thereby ensures & provides the best possible performance and quality to the end-user. Thus, enabling the owner of the vehicle to enjoy good profitability, low maintenance costs and a high resale value.

On the other hand, the modular system limits the number of components being used across the organization, thereby, making the entire production process extremely cost effective. This business model is one of the most important factors making sure that Scania is profitable every single year for the last six decades and is often described internally as a win-win situation in terms of relationship with customers.
The modularization strategy instead of being looked at, primarily, as a model for lowering production costs; is viewed as an essential means of being able to meet both customers and legislation’s demands in the shortest possible turn-around time while simultaneously restricting the number of parts or components being used in the products from growing uncontrollably over a period of time. Modularization, thus, also enables the company to develop new components without having to change the existing components at the same time. Based on the assumption that if the system can reduce the overall number of components across the product range by 50 percent, it lowers the company’s R&D costs by 30 to 50 percent, production costs by about 10 percent and sales and service costs by about another 30 percent. Additionally, the strategy has led to stronger relationships with the customers as a natural outcome of higher interfacing requirements for customization.

“Our business model must not be confused with standardisation. The objective is to tailor solutions for each one of our customers. Modularisation begins and ends with the customer. Every vehicle we deliver is specified – put together – with an eye to a unique customer’s driving pattern, industry, legal environment, local topography and climate.” elaborates Anders Lundström, Senior Advisor at Scania.

The process utilizes two set of components; one, the standard interfaces or connecting points which are kept standard across products and second, the performance steps which are customized based on customer needs. “The development of new performance steps is driven by customer needs and legislation. For instance, today we are seeing different emission laws in different parts of the world, and this is driving engine development – which for us means supplementing our existing range with additional performance steps. For example, we have added more and more engine performance steps and today we have steps from Euro 3 to Euro 6 emission requirements. This flexibility gives us competitive advantages compared to standardised solutions.” Says Staffan Sjöström, Engineering Director/ Head of Vehicle Definition.
The modularisation has been largely responsible for the company’s decent performance during the current global economic slowdown as despite a sharp drop in demand during 2009, the company has been able to scale-down production rapidly in order to meet the demand levels effectively. The system also provides potential synergies & interoperability between bus and truck manufacturing, as about 85 percent of the components in a tourist coach chassis are shared with a truck chassis.
**Well-balanced portfolio spread evenly across products & services – a Natural Hedge**

Scania has a well-developed & diversified portfolio spanning across products & services giving it an edge over closest key competitors.

The portfolio consists of:

- Trucks Manufacturing
- Buses Manufacturing
- Engines Manufacturing for Marine & Industrial applications
- Service related Products
- Used Vehicles
- Financial Services

In 2009, about 52% of Scania’s gross revenues originated from truck manufacturing as against 65% in 2008 while the service business (including service related products & used vehicle sales) grew from 24% to 33% in terms of contribution to annual revenues although the overall revenues for the year 2009 declined to EUR 6.2 billion (approx.) from EUR 8.89 billion in 2008 as demand plummeted in the Western European truck market.

The well-developed services and aftermarket business put the company in a unique position where the relatively much more stable services revenues proved to be an effective cushion & hedge against the relatively cyclical, trucks manufacturing business. Scania has a well-developed services portfolio & provides a range of fleet maintenance service solutions to a
number of logistics companies in the western European market. During the economic downturn a number of logistics companies decided to postpone any fleet renewal/replacement decisions as a result of the decline in business demand & the decreased capacity utilization led to decline in volumes for maintenance services. In addition, some of the companies also decided to cut down on the number of contractors providing the fleet maintenance services for operational efficiency reasons. Scania being a leading name in the fleet maintenance services business with proven expertise gained on this part too and was selected as a sole provider of fleet maintenance services by some logistics companies. The company also expanded its services range with the addition of ancillary vehicle-related services including repairs, maintenance and spare parts for trailers, superstructures & bus and coach bodies, as well as by enhancing service offering for older vehicles. As a result, on one hand the trucks business shrunk by 41% in terms of annual revenues (EUR 5.5 Billion in 2008 to EUR 3.2 billion in 2009) on a year on year basis while on the other the services business more or less maintained the status quo with a mere 3% decline in revenues on a year on year basis (EUR 1.63 billion in 2008 to EUR 1.59 billion in 2009). The availability of a relatively more stable & well-developed services portfolio was another major factor after modularization which ensured that the company doesn’t see red in its annual results.

Leif Östling, Scania group’s President & CEO too remarked in his comments for year 2009 annual results: “Despite the 41 percent downturn in deliveries and the sizeable increase in credit losses in customer finance, Scania reported positive operating income of SEK 2,473 m. for the full year, due to more stable service revenue and the cost reductions that were carried out.”

**Ensuring Structural Flexibility, Nimbleness & Agility – Key to Managing Tough Times**

Structural flexibility has been a hallmark of the Scania’s overall strategy as demonstrated by the company’s preference for the unique modular production system. During the crisis which started towards late 2008, the company showed remarkable agility in terms of rapidly aligning the production output with the declining market demand, harnessing advantages of the modular production system, reducing inventory levels, downsizing & revamping the overall cost structure.

A total of 3,900 employees were laid off by the Group between September 2008 & December 2009 to maintain competitiveness and the largest cutbacks were implemented across production units. Most importantly, the company was able to effectively narrow down its cost base by reducing the number of working hours across a number of European countries & by introducing a 4-day work week in Sweden. In Sweden, the company introduced a four-day week in June 2009 spanning across & affecting about 12,000
employees, which included a reduction in pay of about 10 percent for the second half of 2009. The introduction of reduced working hours led to potential savings of SEK 300 million till December 31 2009. The reduced working hours continued to remain in effect till April 2010 when the company decided to increase production based on a spurt in demand.

Also, the company restructured the European axle and gearbox production units towards late 2008 which led to potential annual savings of SEK 300 million to be realized from the year 2009.

**Presence in relatively Insulated, Key Growth Markets in Latin America & Asia – Leveraging Market Growth Potential**

Amidst a crisis which had global implications & ramifications; the presence & relative dynamics across markets became a key factor for all the truck-makers as the crisis had differential relative impact on markets. The North American market was the first to fall as the crisis had its roots there & gradually it swept across Western Europe; the world’s two biggest markets for commercial vehicles in terms of values as well as volumes. The relatively smaller but significant markets of Latin America & parts of Asia, especially, China & India, remained almost insulated from the impact of the economic conditions prevailing in the other parts of the world on account of strong domestic demand originating from a sustained growth trajectory across these markets. Thus the relative presence & scale of operations in these key markets which continued to grow during this spate of downturn made all the difference to the bottom-line of all global truck-making companies.

Regarding Scania, the group has had a presence in some of these growing emerging markets especially in Brazil in Latin America & parts of Asia.

As evident in the charts above, the group’s presence in Latin America made all the difference. Brazil continued to be the largest market for the group which continued the growth momentum,
driven by strong growth in the natural resources exploration industry. The performance in Brazil, partially offset the situation prevailing in other major markets for the group & helped save the bottom-line to some extent.

**Market Dynamics for Scania’s Truck Business – New Truck Registration Numbers & Market Share**

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**Conclusion**

The case, firstly, highlights the significant advantages of creating as well as ensuring structural balance & flexibility in an organizational context, in addition to demonstrating & showcasing - as to how, by leveraging the structural competitive advantages while simultaneously staying nimble & agile in terms of managing strategic changes; an organization can effectively manage any major unexpected industry or economic downturn. The Scania group, as a result, has once again been profitable for the year 2009 & even has proposed a dividend to the investors in an industry environment where all major European truck manufacturers including the likes of Daimler (world’s largest truck-maker), Volvo & MAN booked losses in a year which the global trucking industry will not be able to forget; yet would not like to come face to face with, ever again.
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