Eight transforming trends in the commercial aftermarket

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White Paper

The commercial vehicle aftermarket is rapidly changing, and market dynamics affecting distribution channels, technology, product and service offerings will alter the way we do business. These changes can positively influence our course of action if they are embraced with the careful preparation that is necessary to capitalize on them. Being aware of what is coming next is essential to future success. Here is a look into current trends impacting our industry.

1. Technology is rapidly changing, making it easier to be in the "know"

Technology often can be overlooked as a buzzword, but for the commercial vehicle aftermarket, it carries some very heavy weight behind it. For instance, 10 years ago, telematics in the commercial vehicle segment was dominated by one supplier – Qualcomm. Today, the market has countless solutions for collecting and tracking fleet data. This feature is offered by various types of suppliers: from traditional technology firms to independent distributors, marketed under Omnitracs Analytics, PeopleNet Fleet Manager, CarrierWeb® Fleet Management, and Fleetmatics. Manufacturers recognizing this opportunity have created their own solutions, including OnCommand™ by Navistar and DetroitConnect by Daimler Trucks North America. Furthermore, dealers, distributors, and marketing groups understand the critical need for data collection from these telematics systems, which can be used for inventory planning and maintenance scheduling for example. Options from this group include HDA Truck Pride with iMatics and Rush Truck Centers with GeoTab.

The collection and interpretation of data can be invaluable for the truck owner and a source of revenue for the telematics provider. An enormous amount of data is collected – up to a couple of hundred sensors per vehicle provide ongoing data. According to Terry Cline, CIO for Navistar Inc. in a recent Wall Street Journal article, Navistar's OnCommand systems collect "20 million records per day from its customers and other data sources." [1]

[1] Kim Nash, Truck Maker Navistar Says Open Data Expands Market for Analytics Service, The Wall Street Journal, 6 January 2016

Data collected from telematics help provide information on prognostics and preventative maintenance, which enables users to recognize issues earlier, so part failures can be addressed. There are also the future possibilities of Vehicle-to-Vehicle (V2V) connectivity, in which trucks can exchange data with other nearby vehicles in order to better understand the road environment, thus avoiding accidents, closed lanes, and much more.

For OnCommand, the data collected from these trucks has translated into a direct improvement in costs. In fact, OnCommand customers saw maintenance costs drop an average of 30 percent[2]. There are few technologies that can have such a direct impact on a fleet's bottom line, and this is why the industry can expect the use of telematics systems to increase.

Telematics, although still fairly new in this industry, is expected to become a $50 billion market opportunity by 2020, with North America being the highest generating market.[3]

Of course, telematics is not the only technology impacting the commercial vehicle business. Here are a few others to keep an eye on:

- Emissions control systems are competing with tires as the number one expense for some fleet owners.
- An increase in the use of collision avoidance systems will reduce the need for replacement parts.
- All-makes diagnostics will continue to help address the right to repair.

CarrierWeb is a registered trademark of CarrierWeb L.L.C.
OnCommand is a trademark of International Truck
[2] Kim Nash, "Truck Maker Navistar Says Open Data Expands Market for Analytics Service," The Wall Street Journal, 6 January 2016
[3] Sonali Hansda, "World Commercial Telematics Market - Opportunities and Forecasts, 2013 – 2020," Allied Market Research, April 2015

- As 3D printing becomes more readily available, it has the potential to be a future game changer for the aftermarket business model, allowing service centers or distributors to produce some common parts by printing them.
- And, finally, over-the-air software updates will begin making upgrades to infotainment, navigation systems, and electronic systems.

2. Consolidation is growing in nearly every area of the commercial vehicle market

The second major trend in the commercial vehicle market is consolidation. The opportunities are significant and private equity firms have played an important role in investing in the industry as they secure stakes in key companies, including AxleTech International.

There are many examples of consolidation in nearly every area of the market. Tier 1 suppliers, including Stemco, ConMet, and Rome Truck Parts, have all come together while Trucklite and Federal Mogul have significant private equity ownership structures. Dealers such as MHC, Rush, and Truck Country have acquired numerous smaller dealers and are continuing to grow into what could be considered megadealers. Even from the independent aftermarket side, PowerTrain, TruckPro, and Crane Carrier Corporation have merged, and these types of changes have even impacted well-established brands such as Weller, Jasper and TransAxle.

One thing is certain – there is even greater potential for consolidation in the future, especially as it relates to the dealer groups. Aging owners seeking a way to retire, as well as to reduce overhead costs by consolidation of back-end operations, are more likely to consider consolidation.

In addition to the consolidation of these companies, there is also a convergence of automotive and heavy truck markets, especially as it relates to the ability to service the entire vehicle fleet. HDA Truck Pride has historically focused primarily on heavy trucks; however, the company recently made an announcement to form a new joint venture

with Aftermarket Auto Parts Alliance (AAPA) to better serve customers in the "light-, medium- and heavy-duty truck markets."[4] The coordination of the heavy truck and the traditional automotive markets will present some unique opportunities for cost savings and efficiency across distribution networks.

3. Distribution is shifting away from the traditional business model

Distribution in the commercial vehicle aftermarket has not significantly changed in quite some time, but that run is over. According to a recent report by the Autocare Association, e-commerce in the automotive aftermarket is the fastest growing channel for distribution and is expected to double in size to $13.2 billion by 2018, up from $6 billion in 2013[5]. As has been observed time and again, trends that aggressively start in the light vehicle market often make their way into the commercial vehicle industry. The report also indicated that the automotive aftermarket e-commerce business is doubling in size every five years – making it a significant trend.

Because of new industry dynamics, including the rise of megadealers and e-commerce, the historic rules of the commercial vehicle aftermarket are changing rapidly. With the distribution model becoming much less restrictive, it is possible that the methods for delivery will change, making it easier for innovative thinkers to bring in new ideas on how to make the business model more efficient, user-friendly, and especially cost-effective.

Amazon has established itself as one of the largest and most well-known online retailers in the business-to-consumer space and they are aggressively pursuing business-to-business as a growth driver. The automotive sector is a significant and growing segment, which is a telling sign for a company that brought in $107 billion in 2015[6]. The company is well positioned for distribution, too, with over 70 fulfillment centers across

[4] Tire Business Staff, "HDA Truck Pride, AAPA create new alliance," Tire Business, http://www.tirebusiness.com/article/20160418/NEWS/160419928/hda-truck-pride-aapa-create-new-alliance,18 April 2016

[5] Autocare Association, "e-tailing in the Automotive Aftermarket," September 2014

[6] Amazon Press Release, "Amazon.com Announces Fourth Quarter Sales up 22% to $35.7 Billion," http://phx.corporate-ir.net/phoenix.zhtml?c=97664&p=irol-newsArticle&ID=2133281, 28 January 2016

the U.S.[7] This means they can quickly address same-day delivery, but even more interestingly, they have already started creating fleets of drones, hiring drivers for deliveries, and are pushing legislation for longer trucks. This opens the door to the possibility of significant changes in both the speed and method of distribution.

While the means for finding parts is changing with e-commerce, the way in which products are actually delivered door-to-door could also change in the near future. For example, take the opportunity that drones present in package delivery. This may reduce the need for delivery trucks, as these drones will help speed up the delivery method to customers, and fewer miles equates to less maintenance. Additionally, fleets will have access to this ordering system, making it a double threat by reducing the need for trucks, and enabling quicker delivery of parts ordered online. In fact, according to RadianInsights, in just 7 years, unmanned aerial systems will increase to $4.8 billion[8], making them a serious opportunity for distribution channels, assuming they overcome regulatory approvals in the near-term.

Beyond online purchases, the consolidation in the industry is creating megadealers capable of buying directly from manufacturers. These megadealers have significant purchasing power and seek opportunities to buy more products direct. As a result, the need for the traditional distribution system will change. The largest megadealers are opening more locations and other small-to mid-sized fleets can expect to consolidate with larger ones, opening further direct-buying opportunities.

4. Remanufacturing is expanding to electronics

It is not surprising that remanufacturing is on this list, but the most interesting change in this area is the fact that electronics is one of the highest growth segments in remanufacturing.

[7] Amazon, http://www.amazonfulfillmentcareers.com/amazon-fulfillment/locations/
[8] "Commercial Drones: Highways in the Sky, Commercial Unmanned Aerial Systems (UAS),Market Shares, Strategies, and Forecasts, Worldwide, 2015-2021," WinterGreen Research, http://www.radiantinsights.com/research/commercial-drones-highways-in-the-sky-commercial-unmanned-aerial-systems-uas-market, 9 January 2015

According to Joe Kripli, president of the Automotive Parts Remanufacturing Association, “Electronics now represents over 30 percent of the average automotive vehicle’s content, and commercial vehicles are heading in the same direction.”

It is a significant growth area for the commercial vehicle market, but it is also highly specialized. Some of the biggest brands are becoming key players, including Detroit Diesel, Caterpillar, Cummins, Delphi and Robert Bosch. Electronics could begin to compete with powertrain components for the fastest growing area in remanufacturing. Consulting firm Frost and Sullivan recently reported that remanufacturing of commercial vehicle powertrain and safety electronics is expected to grow to $385.5 million by 2020[9], with a large share of volumes coming from ECMs, ECUs and TCUs.

As the quantity of electronic components continues to grow in commercial trucks, remanufacturing of these components is expected to grow also.

5. All-makes as a winning strategy

Many market participants are pursuing the all-makes approach as they find their partial offerings are not fulfilling industry demands. On the other hand, this can be a very confusing and challenging situation for fleet owners. The all-makes offering will trigger the establishment of a quality standard that fleets can come to expect, as the current market – filled with a myriad of brands – is not giving them confidence in genuine quality. In the near future, the demand for genuine quality products will increase and this will significantly impact the all-makes strategy for the better.

One way to counter this trend is through investment in brick and mortar, which helps build confidence that a brand is well established and of high quality. A great example of this is PACCAR’s TRP brand, which opened five store fronts in 2015, with opportunity for future expansion. These store fronts are also expected to include service centers for the convenience of its customers.

[9] “Electronics remanufacturing is a growth area in the heavy duty commercial vehicle aftermarket,” Vehicle Service Pros, http://www.vehicleservicepros.com/article/12029993/electronics-remanufacturing-is-a-growth-area-in-the-heavy-duty-commercial-vehicle-aftermarket, 10 February 2016

6. Service is becoming an essential source of growth for distributors

According to MacKay & Company, the number of service centers is expanding, becoming a significant growth area for distributors. The total Class 6-8 aftermarket represents $107 billion, with half – $53.5 billion – on service labor. While parts ($30 billion) and tires ($16 billion)[10] are a significant part of the total aftermarket, they are insignificant in comparison to the size of the service portion of the business. As a result, we can expect more and more aftermarket distributors to capitalize on this opportunity by opening service bays and repair centers.

7. The growing importance of training

A number of technologies were highlighted in the first trend covered in this paper, many representing new capabilities for service technicians, so these technologies are going to drive the need for additional training. Software, electronics, and emissions changes are requiring repair shops to learn different types of repairs. While fleets and dealers expect free training, the independent workshops have less access and are becoming more critical to the aftermarket – as the demand for service increases. Selling training to these independent workshops, and eventually the fleets, will become a bigger part of the business model, especially from big manufacturers who are going to look toward training for revenue. There are even some major parts suppliers starting down this path, helping to train on the complex systems they deliver to improve serviceability and drive revenue growth.

8. OEMs will continue insourcing

Original Equipment Manufacturers (OEMs) are continuously looking at new opportunities to increase revenue and market share. In the past, there were a few major suppliers in transmissions and axles, including Dana, Meritor, Eaton, and Allison. Today, OEMs, including Volvo with the i-shift, Mack with the m-Drive, and Detroit Diesel with the DT12, are all competing in this space – adding complexity in the market for

[10] MacKay & Company, 2016

training, repair, parts availability, and much more. Fleets prefer consistency across their trucks for simplified ordering of replacement parts.

In conclusion, the commercial vehicle aftermarket appears to be in a constant state of change, and while some of these trends are challenges, they also certainly present great opportunities. From new technologies and industry consolidation, to the offering of services and training, it is important that each company evaluate its current portfolio of products and services to ensure it remains ahead in this ultra-competitive aftermarket landscape.

AxleTech International, based in Troy, Michigan, is a supplier of off-highway and specialty vehicle drivetrain systems and components to original equipment manufacturers and the aftermarket for commercial and defense customers around the world. AxleTech has nine vocational markets: agricultural, aircraft ground support, construction, forestry, material handling, defense, mining, specialty truck, and transit. AxleTech has manufacturing, distribution, and engineering facilities in Oshkosh, Wisconsin, Chicago, Illinois, Saint-Étienne, France, Osasco, Brazil, and Pune, India. For more information on AxleTech International visit www.axletech.com.