

# Volvo and Geely

Phil Waterhouse explains the success of the Swedish car company since it was bought by Chinese firm Geely

Understanding which car manufacturer owns which is not always easy, given the levels of acquisitions and mergers that take place within the industry. At the time of writing, the five largest manufacturers are:

- Toyota
  - Volkswagen (VW)
  - Hyundai
  - Ford
  - General Motors (GM)
- The top five manufacturers produce over 40 million vehicles a year, and all own various other brands. The temptation for mergers and takeovers within this industry is based on exploiting economies of scale, integrating supply-chain management systems and establishing bases within different areas of the global market. However, mergers and acquisitions within the industry can be especially fraught, as witnessed by the troubled unions of Daimler and Chrysler, GM and Saab, and Ford and Jaguar.

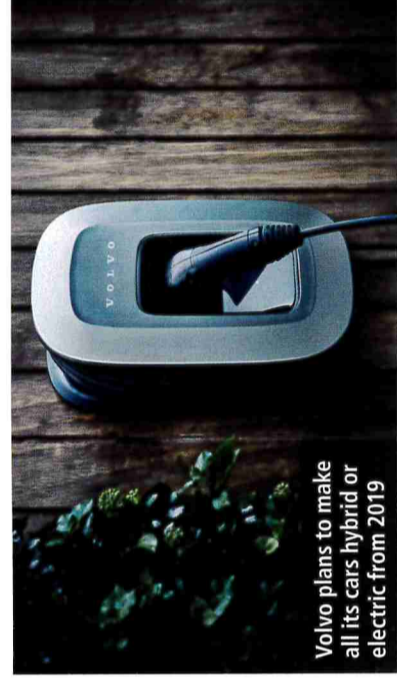
Following the fire-sale of Volvo by Ford to Chinese-based Geely in 2010, some incredible results have been produced by the new company that serve as a lesson to other businesses looking to expand their product portfolio by taking over rivals.

## Little Volvo

Volvo has been a byword for safety over its 91-year existence. It was responsible for the standard three-point safety belt that all cars now have, and has a reputation for durable, reliable — albeit rather box-shaped — vehicles. On a recent trip to Sweden I was amazed at the sheer numbers of Volvos on the road, some more than 30 years old and still going strong.

While popular in its home country, the company has struggled over the years to grow and develop its brand. This is partly down to the relatively small scale of operations it has against its larger rivals. The company was traditionally positioned between cheaper mass-produced cars and premium brands. The smaller volumes that it sold at relatively modest margins compared to the more prestigious brands such as BMW and Mercedes meant that it could only make small changes to its designs year on year. It was unable to significantly increase prices to obtain extra funding for research and development (R&D).

This put the company in a difficult position and left it vulnerable to a takeover, which duly arrived in 1999 when Ford paid \$6.5 billion for the brand. The idea was that Ford could streamline operations and centralise certain aspects of the car



Volvo plans to make all its cars hybrid or electric from 2019

production. Much of Volvo's design work was taken in-house by Ford. However, Volvo did manage to access a portion of Ford's R&D budget, and with this it decided on what turned out to be an inspirational decision.

Volvo invested these funds in creating just one type of engine — a four-cylinder version. Its upmarket rivals were developing multiple versions of their engines with different numbers of cylinders, as the feeling was that more cylinders equals more power and therefore more consumer demand. However, by just focusing on one type, Volvo was creating an engine that could be continuously improved. This caught the attention of Geely, a relatively small Chinese manufacturer.

## Investment pays off

The owner of Geely, Li Shufu, liked what he saw. Volvo seemed to have something his company did not — namely expertise in technology, R&D, design and operations. Geely was known as a 'me-too' car manufacturer, producing knock-off, cheap versions of cars to attract first-time buyers within its domestic market.

Li felt that Ford was not fully valuing the potential of the Volvo brand. When he offered \$1.8 billion for it in March 2010, Ford readily accepted, as sales had fallen to 335,000 from a peak of 458,000 in 2007. Ford executives felt they were getting rid of an underperforming product within their portfolio.

The genius of the acquisition came with what Li did next. Many experts thought that Geely would create cheap, low-grade Volvos akin to fake Rolexes. After all, Geely had come dead last out of a survey of all 36 Chinese car manufacturers. However, from the start of the takeover, Li made it clear that the two brands would operate completely separately, and that Volvo's still predominantly Swedish management team would be left unchanged and they would work without any interference from China.

Li was good on his word. With the extra backing that he provided to the company, it was finally able to innovate and come up with the freshest car designs in its history. The new versions of the V60 and XC90 have been met with hugely encouraging reviews in terms of both performance and looks. In 2017 the company sold a record 570,000 cars with an operating profit of over \$1.75 billion. Not a bad turnaround for a company that had been sold off so cheaply just 7 years previously.

## Expanding overseas

This turnaround in financial performance has led to what was always likely to be a part of Li's strategy. He wanted to give the existing company the space to turn itself around within 5 years by

giving it financial support, and more importantly the freedom to do so without interference.

However, now this has been achieved, he is beginning to push the company further into the Chinese and US markets. The new purpose-built Volvo production facility in South Carolina, USA, is very much a nod to corporate social responsibility and the future move to electric-only vehicles. The plan is for the company to reach a production capacity of 150,000 vehicles in the USA and create employment opportunities for 4,000 workers. With President Trump focused on protectionist policies and encouraging American citizens to buy American-made products, locating within the country and creating jobs is a way for Volvo to circumnavigate these issues.

At the same time, the company has opened two further production facilities in China. This means that it benefits from lower labour costs and Geely's relationships with local suppliers, does not pay import tariffs, and saves on shipping costs. The Chinese market has become the firm's biggest, selling 100,000 cars a year — more than it sells in Sweden.

Volvo and Geely are now beginning their first proper joint venture, launching a new line of vehicles under the brand name Lynk & Co., positioned between the Geely and Volvo brands. While not quite Tesla, there were already 6,000 orders before production started.

## Electric future

When Volvo announced that it would be going fully electric on all new models from 2019, this attracted a lot of positive PR and column inches around the world. This was a clever move, as it was built on the fact that Geely had been working on developing electric motors independently for the past decade.

When you investigate the details slightly further, what Volvo and Geely are promising looks more like a fully hybrid or electric future from 2019. While they will bring out fully electric models, most of the profits will come from cars which still have a traditional engine but also use an electric motor, e.g. for urban and low-speed driving. This is in line with the strategies that rival manufacturers will be adopting until at least 2025.

Ultimately though, the industry will have to go fully electric in time. This is a further area where Geely and Volvo can be seen to have stolen a march over their rivals, both through the announcement of their plans and the actual cars they are designing and making.

Tesla has a valuation of over \$58 billion and this is 25% higher than that of Ford. However, Tesla is yet to actually make any profit from its cars and has been struggling to scale up operations to reach its production target of 20,000 cars a month. Volvo and Geely have quietly gone about working through these issues and scaling up production.

The success of the Volvo acquisition has led Li Shufu to investigate other investments, and he has recently become Daimler's largest shareholder. While it is perhaps unlikely that Volvo will overtake previous owner Ford, its example does show how one company's problem child can become another's star performer.

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