

ENVIRONMENTAL ANALYSIS OF AN INDUSTRY

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1 Introduction

The report explores some of the key external developments affecting the performance of Volkswagen. In general, external political, economic, social, technological, environmental and legal shape the internal business environment by delivering certain opportunities and threats to business organisations (Johnson et al., 2017). As a result, large multinational enterprises, such as Volkswagen, cannot overlook the relevant trends which may support or inhibit important aspects of doing business, including trade conditions, consumer preferences, manufacturing conditions and others (Morrison, 2022). This point was supported by evidence in the previous report showing some of the main challenges for the automobile sector in the contemporary business environment, including the war in Ukraine, pandemic supply chain restrictions, consumer changes, economic difficulties and regulatory changes.

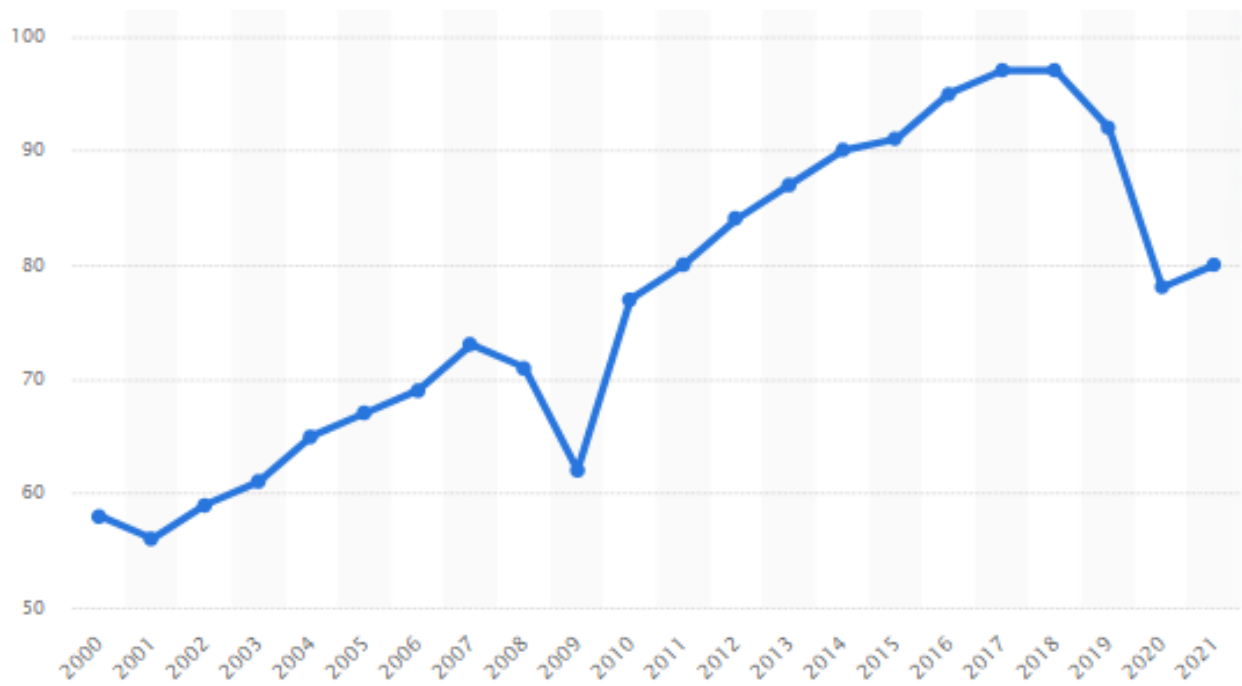
The purpose of the current report is to more closely focus on the pandemic-related developments which have shaped the business environment in the last two years. The analysis is critical by outlining not only the negative effects of the pandemic, but also some trends with a positive role for the transformation of the automobile sector. After the completion of the critical evaluation, a set of factors for survival and success is explored, so that Volkswagen is able to reflect the megatrends as a part of its strategic development process. Thus, some main directions for future success could be elaborated accordingly.

2 Effects from the pandemic

2.1 Negative effects

The negative effects of the pandemic are clearly seen in 2020 and 2021 when the demand for automobiles continued to be significantly lower in comparison to the pre-pandemic levels (Placek, 2022). As shown below, sales of vehicles declined by more than 20% and stabilised at lower levels due to a combination of pandemic-related factors, such as uncertainty, economic difficulties, supply chain issues and closures of dealerships (Hensley et al., 2021; Placek, 2022). This is a major challenge for the industry and Volkswagen in particular, as reduced sales also cause worse financial performance in terms of profitability and growth.

Figure 1 – Global production of automobiles (million)



Source: Placek (2022)

Special attention should be placed on supply chain issues, as they appear to be quite persistent. The pandemic has led to closures of many harbors and transportation disruptions (Reuters, 2022). These negative developments have caused production delays and higher production costs due to the shortages. The supply chain issues have been particularly severe in relation to findings chips – a key component in automobile manufacturing (Fitch, 2022). Due to the pandemic disruptions, chip production is not expected to recover before the end of 2024, as suggested by current projections (Fitch, 2022). In this light, it is unlikely for the industry to reach the pre-pandemic production levels, even if there is strong consumer demand. The rapid increase in the price of new and used vehicles is another manifestation of the existing supply shortages in the automobile industry. This is evidenced by Ulitskaya (2022) who shows a dramatic 48% price increase of used cars in comparison to a year ago.

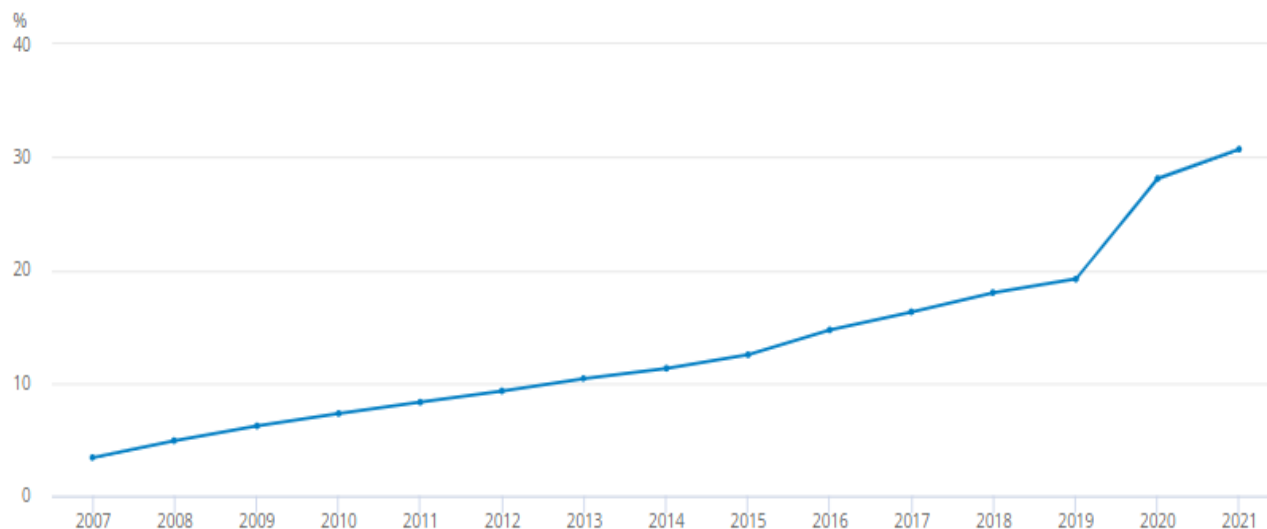
2.2 Positive effects

Despite its negative effect on the sector, the pandemic also promoted positive changes. As argued by Hensley et al. (2021), automobile companies focused their efforts on accelerating the

technological transformation as a way of boosting productivity and resilience amid the external challenges. In particular, there have been improvements in supply chain monitoring and visibility, so that automobile companies are better able to avoid shortages of raw materials and components (Hensley et al., 2021). Moreover, supply chains are in a process of transformation by considering a wider range of suppliers, shortening of supply routes and accumulating inventories of key components in order to avoid costly shortages and inefficiencies in the future (Hensley et al., 2021).

The second major transformation has taken place in terms of sales channels. The pandemic led to a closure of many dealerships; thereby, demonstrating the inappropriateness of solely relying on physical distribution channels. As a result, digital channels have been developed in order to support the performance of physical ones, so that the automobile companies are able to benefit from the e-commerce growth during the pandemic (Hensley et al., 2021). The growth of e-commerce has been a major trend, as shown by the share of online sales which already exceeds 30% of all retail activity (ONS, 2022). In this light, e-commerce clearly delivers previously ignored (except for the case of Tesla) channels to sale products and communicate with customers.

Figure 2 – E-commerce share of all retail sales in the UK (%)



Source: ONS (2022)

The third positive effect, which can also be considered as a mega trend affecting all industries, refers to the emergence of sustainable consumerism. According to Deloitte (2021), 85% of UK

consumers express willingness to adopt a more sustainable pattern of behaviour. This leads not only to a changed shopping behaviour in terms of reducing the use of plastic and other unsustainable products, but also to stronger preferences for brands which demonstrate sustainable and ethical behaviour in the marketplace, as suggested by 34% of survey participants (Deloitte, 2021). The increased environmental awareness of consumers has also promoted positive changes among automobile producers which have already focused on increased investments in electrification of vehicles, shared mobility, smart design and others (Hensley et al., 2021).

3 Survival and success factors

3.1 Change culture

The first success factor is more general but quite impactful on organisational performance in the long-run. It is related to the development of an organisational culture which promotes change and continuous development. A change culture incorporates effective leadership, effective goals and vision for the future, as well as change-oriented attitudes and behavioural norms by employees (Huczynski and Buchanan, 2013). As a result, a culture of change is expected to weaken the complacency and pursue valuable goals for becoming more innovative, flexible and competitive in the marketplace (Huczynski and Buchanan, 2013).

A culture of change is justified by the turbulent external developments related to the pandemic, economic trends, volatile consumer preferences and others, as discussed in the external and industry analyses. In this relation, existing business models may no longer be appropriate in the future and companies have to adapt accordingly to the emerging changes in order to stay competitive. Therefore, Volkswagen's strategic success largely depends on the organisation's ability to change but this may be an issue given the large size of the organisation which slows down decision-making and changes as a whole.

3.2 Sustainability and technological upgrade of value chain

In alignment with the earlier mentioned organisational culture of change, Volkswagen's success would also depend on the organisational ability to incorporate sustainability and technological changes. As discussed, these are key megatrends which have accelerated during the pandemic.

Respectively, Volkswagen has to more closely apply them as a part of its value chain in order to adapt to the evolving mega trends.

The value chain model explains the stages of value creation by taking into consideration a set of primary and secondary activities (Porter, 1990). Focusing on all parts of the value chain ensures a profound change which incorporates the megatrends for sustainable development and technological progress.

Figure 3 – Value chain model



Source: Mind Tools (2022)

Volkswagen depends on the supply of raw materials, components and other supplies for the production process; however, the shortages of chips is one of the main issues worsening inbound logistics of the organisation and it should be addressed by changes in the supply chain (Volkswagen, 2021; Burgess, 2022). Similarly, the geopolitical tensions have closed some of the manufacturing sites responsible for the outbound logistics of the organisation (Burgess, 2022). Given these logistical issues, Volkswagen is advised to shorten its supply chain, re-consider

production locations as well as implement new technologies which minimise the dependence on suppliers.

In terms of production, the company maintains a production volume of more than 30,000 vehicles per a working day (Volkswagen, 2021). Significant success has been achieved towards a more sustainable development in the field of production. In comparison to 2010, Volkswagen has managed to reduce carbon dioxide emissions per produced vehicle by 33.3%, whereas water and waste have been reduced by 11.6% and 61.6%, respectively (Volkswagen, 2021). More efforts are necessary in terms of energy consumption reduction where the progress for the decade is only a reduction of 3.5% (Volkswagen, 2021). Despite the performance weaknesses, Volkswagen has achieved a gradual success in improving its sustainability performance. As shown below, the brand improved its sustainability rating in two out of three key rankings (Volkswagen, 2021). For the purpose of the critical analysis, it should be noted that significant additional improvement is necessary to place Volkswagen among the sustainability leaders in the automobile sector.

Figure 4 – Sustainability ranking of Volkswagen

	2019	2020	2021	
MSCI 	CCC	CCC	B	↑
 SUSTAINALYTICS a Morningstar company	41.4 (severe risk)	41.7 (severe risk)	29.6 (medium risk)	↑
ISS ESG 	C	C	C	→

ESG rating scales

Source: Volkswagen (2021)

In the other areas of the value chain, Volkswagen demonstrates commitment to improve its research and development capacity by increasing its technological investments by €89 billion (Volkswagen, 2021). This is a key policy which reflects the increasing speed and scope of technological change in the industry. Hence, the intended investments in new technologies are a key for success and survival in the long-term.

There are also stated initiatives aiming at improving the performance of marketing and sales, as well as service; thereby, meeting the changing needs of customers – an important stakeholder group for Volkswagen (Volkswagen, 2021). Nevertheless, the company lacks clear policies in fields, such as firm infrastructure and human resources. Hence, more efforts are necessary to fully cover all areas of the value chain process. In particular, the focus on human resources is suggested to be quite relevant for Volkswagen in the light of the proposed organisational culture change, the importance of employees as a stakeholder group, as well as the key role of qualified professionals in determining the performance of the company over time.

3.3 Stakeholder management and corporate social responsibility (CSR)

A key factor for success and survival in the long-term is also the ability to understand and address the needs of different stakeholder groups. By definition, stakeholders are individuals and groups who may influence or are influenced by the operations of an organisation (PMI, 2017). Hence, the support and approval of stakeholders is necessary for achieving long-term success. This is also clearly proposed in the Stakeholder Theory by Freeman (1984) who argues that the sole focus on profit maximisation to satisfy shareholders, as a traditional approach to doing business, is not enough for sustainable success. Instead, companies have to consider the needs of other internal and external stakeholders, such as delivering the best human resource policies to employees, satisfying regulators, cooperating with suppliers and business partners, supporting communities and engaging in societal projects as a part of corporate CSR policies (Freeman, 1984). This proposition of an extensive stakeholder management is also a part of the CSR pyramid model by Carroll (2016), as shown below. The model recognises the importance of various ethical and philanthropic activities in order to address broader needs of the society and strengthen sustainable brand development through CSR activities (Carroll, 2016).

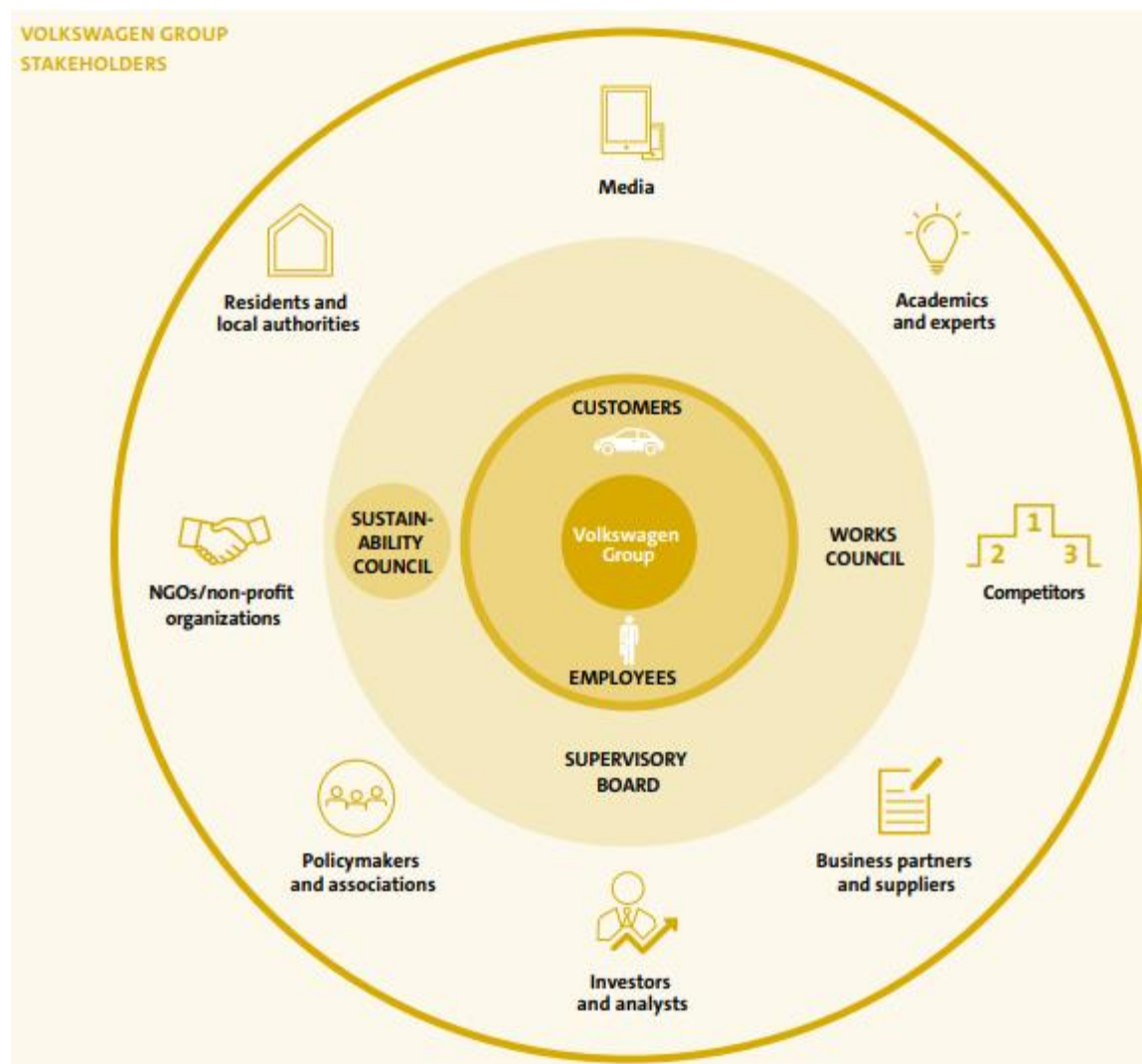
Figure 5 – CSR pyramid model



Source: Carroll (2016)

These propositions by theory are also quite relevant at the current stage of development, given the earlier mentioned interest in sustainable development by an increasing number of consumers (Deloitte, 2021). In this relation, long-term survival and success would largely depend on delivering sustainable products and services in the marketplace and meeting the needs of stakeholders. Currently, Volkswagen identifies numerous stakeholder groups which are positioned in two distinctive layers (Volkswagen, 2021). The most focused efforts are placed on meeting the changing needs and preferences of customers and employees who are considered as key stakeholders for success (Volkswagen, 2021). External stakeholders are many, as they include academics and experts, competitors, policy makers, authorities, media partners, NGOs and others (Volkswagen, 2021). Three organisational units – sustainability council, supervisory board and works council – are developed to analyse stakeholders' needs, implement policy solutions and changes which maximise the satisfaction of the involved parties (Volkswagen, 2021).

Figure 6 – Stakeholders of Volkswagen



Source: Volkswagen (2021)

In this light, the company appears to deliver considerable resources and attention to the critical success area of stakeholder management. Nevertheless, it is unclear why investors, who essentially have a stake in the Volkswagen's ownership, are considered as a part of the external stakeholders, rather than being more closely involved in the decision-making process. Moreover, Volkswagen is a global public company which makes stakeholder management more complex given the existence of ten distinct stakeholder groups with diverse interests (Volkswagen, 2021). In this relation, the company has to consistently evaluate changing needs and find the balance between often contrasting interests of the involved groups.

4 Conclusion

The findings from the report demonstrate the significant changes in the external environment and the role of the pandemic as a catalyst of change. Volkswagen cannot operate in isolation for the surrounding environment; hence, the future strategic success of the brand would largely depend on its ability to change accordingly. In this relation, the development of a culture of change, improved stakeholder management, as well as focus on sustainability and technological implementation is considered as key success factors for the future. The evidence shows the progress of Volkswagen in many of the stated key areas; however, more efforts and consistent efforts are necessary in the future.

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