

Farsky, Mario; Feldhäuser, Julian; Harries, Ferdinand; Levin, Andrej; Papies, Dominik

Article

Car Selling Without Price Negotiations: Wishful Thinking or the New Normal?

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Marketing Review St.Gallen

Consumer Reviews



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Erfolgreich gegen den
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Car Selling Without
Price Negotiations –
Wishful Thinking or the
New Normal?



Car Selling Without Price Negotiations

Wishful Thinking or
the New Normal?

Leading car manufacturers are considering a shift to fixed, non-negotiable prices through direct sales. It is unclear, however, how consumers would react. Based on an empirical study of 500 consumers, this study finds that, while 2/3 of respondents would enter price negotiations, 2/3 would also be willing to pay a mark-up to avoid them.

Dr. Mario Farsky, Julian Feldhäuser, Ferdinand Harries,
Dr. Andrej Levin, Prof. Dr. Dominik Papies

For decades, global car manufacturers have outsourced large parts of their sales and distribution activities to dealers. This continues to be the case in 2023. In fact, most of the pre-purchase process (e.g., providing information, offering test drives) is handled by dealers. Importantly, dealers also have full pricing authority, and it is not uncommon for potential customers to negotiate with multiple dealers of the same brand to obtain the best price.

In recent years, new entrants to the automobile market (e.g., Tesla) have started to use a direct sales model with non-negotiable prices, entirely bypassing traditional dealers. Attracted by the prospect of a single fixed price, less intra-brand competition, and lower distribution costs, incumbent brands have also started to consider this sales model. Especially since the beginning of 2023, incumbent manufacturers have directly witnessed how Tesla is able to enforce sales steering levers (including price adjustments) through its direct sales model, while also seeing how much more cost-effective a direct sales model can be.

It is, however, unclear how consumers will react to such a major shift in the pricing model, which pricing model they prefer, and whether a move to a direct pricing model will help or hurt the performance of incumbent brands. Previous research provides some guidance but has not addressed this specific question. Stigler (1961) highlights the relevance of price information and consumer search for market outcomes, and consumer search for the lowest price will likely be affected by the shift in the pricing model studied in the present research. Zhang et al. (2021) show that consumers may perceive price negotiations as cumbersome, unpleasant, and time-consuming, but they may also appreciate the opportunity to save costs on their car purchases and may view the time and effort they invest in negotiations as worthwhile. Since steep discounts of up

to 30% have been common in the market for decades, it is unclear how customers would respond if these discounts were eliminated all at once. So far, neither academic research nor management publications have empirically explored these questions (for related literature, see Desai & Purohit, 2004; Huang, 2020; Jindal & Newberry, 2018).

What adds to the complexity of the decision is that, on the surface, it seems to be primarily a change in pricing. In fact, however, it is a major strategic shift from a B2B model, in which manufacturers sell cars to dealers without interacting directly with consumers, to a B2C model, in which the manufacturers (and not the dealers) interact with customers. In theory, dealers are in a position to infer and capture each customer's maximum willingness to pay because they operate directly at the point of sale. Hence, price negotiations can also be seen as a way to price discriminate between different consumer segments (Byrne et al., 2022). In reality, the incentive structure means that dealers may often set prices to meet sales targets rather than to capture customers' maximum willingness to pay. The fact that the move to a direct pricing model fundamentally changes the nature of the retail model and the dealers' role makes a solid empirical foundation particularly important.

To shed light on these questions, this article reports the results of a survey of recent car buyers in Germany and addresses the following issues:

- In the automobile sector, do customers prefer a sales model that involves price negotiations or one with non-negotiable direct prices that are the same for all buyers?
- What are customers' expectations about the magnitude of potential price reductions they can achieve in negotiations with dealers?
- What price has to be offered to customers to make them indifferent between a



Dr. Mario Farsky
Associate Director,
Boston Consulting Group,
Hamburg, Germany
farsky.mario@bcg.com

Julian Feldhäuser
Doctoral Student
at the Chair of Marketing,
University of Tübingen &
Boston Consulting Group,
Munich, Germany
feldhaeuser.julian@bcg.com

Ferdinand Harries
Principal,
Boston Consulting Group,
Munich, Germany
harries.ferdinand@bcg.com

Dr. Andrej Levin
Managing Director and Partner,
Boston Consulting Group,
Hamburg, Germany
levin.andrej@bcg.com

Prof. Dr. Dominik Papies
Professor of Marketing,
University of Tübingen,
Tübingen, Germany
dominik.papies@uni-tuebingen.de

Management Summary

Leading global car manufacturers are targeting a shift to direct sales with fixed, non-negotiable prices, yet consumer responses to such a paradigm shift remain largely unexplored. Our study of 500 consumers reveals that in the current market environment, two-thirds would engage in price negotiations, yet the same proportion would pay a mark-up to avoid this common practice. The findings suggest that a carefully planned transition to fixed prices, slightly below current offer prices, could be accepted by consumers, potentially ushering in a new era in automotive retail.

fixed, non-negotiable price and the status quo (i.e., a negotiable offer price)?

The above discussion shows that a direct sales model comprises two key elements: the transition to direct sales contracts between brands and customers, and the elimination of price negotiations. From a consumer perspective, the most salient aspect of this model is the fixed, non-negotiable pricing. Consequently, this paper focuses on gauging consumer perceptions of non-negotiable pricing and employs the term 'direct sales' as a comprehensive label that encompasses both the concept of non-negotiable prices and potentially the move to direct sales contracts.

The following section briefly outlines the established sales model and the changes brought about by direct sales models pioneered by brands such as Tesla. Subsequently, the results of the empirical study are presented and discussed.

Disruptions in the Retailing Structure

In many markets, the established distribution paradigm in the retail (B2C) new car industry has relied heavily on car dealers. Dealers have carried the burden of nurturing the customer relationship, informing the customer, offering test drives, and more. In most cases, this has also meant that the sales contract was signed between the *dealer* and the cus-

tomers, not between the *manufacturer* and the customer. This has two important implications. First, because the manufacturer is not a party to the contract, it cannot set the price. The dealer does, which means that every dealer may offer different prices for the same car—particularly if dealers operate at different cost levels and potential buyers shop around for the best price. In a pilot study (N = 2,250; respondents from Germany, France, or the UK; self-indicated premium car customers or intenders) conducted in November

2021, prior to the main analysis, 77% of customers indicated that they would actively compare prices between dealers of the same brand. Moreover, buyers use this leverage to negotiate with dealers for better prices—so much so that 38% of all dealers perceive same-brand dealerships as their main competitors (Heuser et al., 2023). Second, because the manufacturer does not sell directly to the buyer, it does not collect and maintain comprehensive, unified data about its customers. Rather, these data are dispersed across dealers, making systematic customer relationship management very cumbersome for the manufacturer. Case in point: The online car marketplace *carwow* processes over 10 million data points per day (Schmidt et al., 2020), while car manufacturers pay for transaction price studies for their own cars. Both implications of the established distribution model are highly undesirable from a manufacturer's perspective.

Greenfield manufacturers such as Tesla entered the market with an entirely different approach. In their direct sales model, the contract is signed between the manufacturer and the customer (often online). The direct sales model offers three potential major advantages:

Main Propositions

- 1 Major car brands are moving towards a direct sales model with non-negotiable prices.
- 2 Consumer reactions to such a strategic move have not been studied.
- 3 This study finds that 2/3 of respondents would enter into price negotiations.
- 4 At the same time, 2/3 of respondents are willing to pay a mark-up to avoid negotiations.
- 5 Customers do not enjoy price negotiations but see them as a necessary evil.

- (1) Greater pricing control. Manufacturers can set prices and retain pricing authority without the risk of intra-brand cannibalization between dealers.
- (2) Better customer experience. Manufacturers can provide a more seamless and personalized process and collect valuable data along the purchase funnel, allowing them to better understand customer preferences.
- (3) Cost savings. Manufacturers can save on commissions, marketing expenses, and other overhead costs. Cross-channel price consistency will further strengthen online sales, which are substantially more cost-efficient.

The apparent success of these greenfield manufacturer initiatives has increased the pressure on incumbent manufacturers to move to a direct sales model. It is, however, unclear to what extent customers will appreciate this move and whether they would be willing to give up the ability to negotiate. Even if most customers don't enjoy price negotiations per se, it is likely that a considerable number of them view negotiating as an efficient investment of time that allows them to get more value for their money.

Asking the Customers

This article uses data collected via an online customer survey in Germany between October and November 2022. After sorting out a total of 197 respondents according to a set of predefined rules (e.g., "speeders"), the final sample included

510 subjects who had purchased, leased, or financed a new car for private use during the 24 months prior to the survey. To ensure that the analysis relied on responses from consumers with recent experience in purchasing a car, responses were invited only from consumers who indicated they were the primary decision-makers in the purchase process.

63% of respondents were male and 37% were female. 62% of respondents indicated that they were the sole decision-makers, and 37% were primary decision-makers who received some assistance. 53% purchased a new car, 26% leased, and 21% financed the car at least partially. The median transaction price was approximately €37,000 for both purchasing and financing customers; the median monthly leasing rate was €280. In terms of price segment, 64% of respondents were volume customers, 35% were

premium customers, and 1% were luxury customers, which is fairly representative of the German new car market.

One way to study customer preferences would be to ask customers directly whether they prefer price negotiations or a fixed, non-negotiable price. However, this approach misses an important nuance about the trade-off consumers face: While they are unlikely to enjoy price negotiations, they are likely aware of the potential cost savings. They may view price negotiations as a necessary evil.

Therefore, this study derives a proxy for *bargaining costs* that is based on the respondents' individual choices between a setting in which prices are fixed and a setting in which they can negotiate. As a first step, respondents indicated which price they would expect after bargaining. This is the expected negotiated price. In



Source: © Adobe Stock.

Lessons Learned

- 1 Customers are used to significant price discounts as a result of negotiations.
- 2 The direct sales model is unlikely to be successful if brands try to enforce current offer prices as non-negotiable prices.
- 3 A move to the direct sales model appears feasible if brands adjust prices slightly below current offer prices.

the second step, all respondents were repeatedly confronted with hypothetical situations in which they were asked to decide whether they would acquire their preferred car model (with a specified manufacturer's suggested retail price, MSRP) from Dealer 1, who offers the model for a dealer-specific, negotiable price that is lower than the MSRP, or from another, identical dealer (Dealer 2) located just as far away and offering the car at a price that is lower than Dealer 1's starting price but is non-negotiable. The fixed price of Dealer 2 was then gradually reduced in each iteration of the question until the respondent ultimately chose the fixed price and thus decided against negotiating. This was then used as the basis for calculating the individual bargaining costs:

$$(1) B_i = ((\text{fix price chosen}_i - \text{expected negotiated price}_i) + (\text{last fix price declined}_i - \text{expected negotiated price}_i))/2$$

The intuition behind this approach is that it derives the bargaining costs (B_i) from the difference between the selected fixed price of Dealer 2 (i.e., the point at which the respondent feels that bargaining is not worthwhile) and the expected price after negotiations with Dealer 1. This difference represents the "pain" experienced by the customer when entering into nego-

tiations. If this difference is positive, then customers would be willing to sacrifice some monetary gain to avoid entering into a price negotiation. Equation 1 uses the mean value of the price difference chosen and the last difference declined to smoothen the effect that might be due to the size of the fixed price steps between the iterations of the question.

Customers who had purchased were shown purchase prices; those who had leased were shown monthly leasing rates. In addition, all prices shown were based on the recent purchase price or leasing rate paid by the respective respondent.

What the Customers Say

Do customers in the automobile sector prefer a sales model that involves price negotiations or a direct pricing model with a non-negotiable price that is the same for all customers? It depends. When asked whether they would try to negotiate further down from the offer price of Dealer 1 (before capturing their price expectations and introducing Dealer 2), approximately 2/3 of all respondents say they would negotiate. This is a clear indication that consumers are well aware of the potential cost savings arising from price negotiations. However, this does not mean that consumers prefer or even enjoy price negotiations. Approximately 2/3 of respondents would be willing to pay a mark-up compared to the final expected price after bargaining if they could avoid price negotiations, which means that, for those respondents, the difference between the selected fixed price and the expected price after negotiations is positive. This indicates that the majority of customers dislike the decades-old status quo, the negotiation-based pricing model. This tendency is particularly pronounced among younger and online purchasers. Among customers under 40 and those who have bought online in the past, the share of respondents willing to

pay a mark-up to avoid negotiations is 75% and 70%, respectively.

What are customers' expectations about the magnitude of potential price reductions they can achieve when negotiating with dealers? On average, customers expect a reduction of approximately 6–7% from the dealer's initial price offer (which is typically lower than the MSRP) when entering into price negotiation. The expectations of customers in the leasing market are even higher—approximately 8%—which has pricing implications that are discussed below. In sum, these observations suggest that customers have learned over the past few decades that price negotiations are the norm and typically result in substantial price reductions. This creates expectations; consumers are unlikely to readily accept any given price posted on a car as final.

Given these observations, what price has to be offered to customers to make them indifferent between a fixed, non-negotiable price and the status quo pricing model (i.e., a negotiable offer price)? Automobile

Customers do not enjoy price negotiations but see them as a necessary evil.

brands would need to make sure that their dealers reduce their offer prices by approximately 4–5% to ensure that customers accept the fixed, non-negotiable price. This can be inferred directly from the survey results based on the average relative difference between the initial offer price and the fixed, non-negotiable price accepted by respondents.

Importantly, the price reduction required to retain the customer base is less than the discount that customers expect in price negotiations, which means that customers are willing to pay some mark-up, approx-

imately 2% of the offer price, to avoid price negotiations. This mark-up averages around €910 for purchasing and financing customers, which could significantly improve price realization and have a substantial impact on automobile brands' profits.

The results also suggest that there is heterogeneity among respondents: Younger respondents are less demanding in terms of the discount that they expect. Customers under 40 expect a 3.5% price reduction, whereas those over 55 expect approximately 5%. One plausible explanation for this is that older customers have learned over the years that negotiations pay off, while younger customers are less familiar with negotiations and the price reductions they can achieve.

Discussion

These findings inform an intense debate in the automotive industry during a critical transition phase. Brands are under pressure from new entrants such as Tesla, who market their cars with central pricing authority, lower sales costs, and no intra-brand price competition, as well as pressure from policymakers and the public to improve the sustainability of their product portfolios. At the same time, brands face the need to maintain strong relationships with their established customer base. Against this background, this research shows that a direct pricing model, which no longer relies on price negotiations between customers and dealers, is feasible without alienating customers. However, it would have to be accompanied by lower prices compared to the original offer. The evidence presented above suggests that simply moving to non-negotiable prices at current price levels does not appear to be realistic.

In addition, the willingness to negotiate, the discount expectations, and the willingness to accept a fixed price differ between customer segments, leading to

additional actionable management implications:

- (1) While most customers would engage in price negotiations, a clear majority would also pay a mark-up to avoid them. This suggests that a shift to a direct pricing model is possible without alienating customers, because most of them seem to view price negotiations as a necessary evil.
- (2) Moving to a direct pricing model requires a recalibration of retail prices. Implementing this shift without taking into account the reduced prices that customers typically expect before signing the contract will likely alienate a substantial share of customers.
- (3) Consumers are heterogeneous, and the manufacturers' responses should be as well. For example, decades of market traditions seem to have shaped customer expectations. This implies that manufacturers have to make sure that experienced, older buyers are taken into account when implementing the strategic shift to a direct pricing model.
- (4) Another example of heterogeneity is that leasing customers appear to have higher discount expectations. At the same time, the leasing contract has more pricing components (e.g., interest rate, down payment, residual value, mileage limit) that the manufacturer can adjust to meet the expectations of this segment.

This research shows that a move to a direct pricing model is possible. A first caveat is that manufacturers must be willing to accept somewhat lower initial quoted prices, i.e., lower than typical advertised prices prior to negotiation. A second caveat is that the conceptual advantages outlined above (price control, better customer experience, lower costs) are not an automatic consequence of the move but will only be realized by manufacturers if they can

ensure an effective implementation of the direct pricing model.

A limitation of this research is that it is beyond the scope of this paper to examine alternative configurations of direct sales models, or legal and institutional aspects of the different pricing and sales models, or country-specific heterogeneity in customer preferences.

Nevertheless, this paper hopefully makes a useful contribution to the literature by shedding light on the potential consumer response to a move to a direct pricing model in the automotive industry. ■



For a further supplementary table to the article, visit:

<https://unisg.link/MRSG-Papies-et-al>

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Additional Details Customer Survey

Brand split

Audi 11%, Volkswagen 11%, BMW 10%, Ford 8%, Mercedes-Benz 8%, Hyundai 6%, Renault 6%, Opel 5%, Skoda 5%, Kia 4%, Dacia 3%, SEAT 3%, Tesla 3%, 17% others.

Survey procedure

We collected the data for this study in an online customer survey in Germany between October and November 2022 using a high-quality panel of a professional German market research firm. Respondents were asked to complete a 10 to 15-minute questionnaire, from which we derived our measures.

To derive our bargaining cost proxy as described in the main text, we presented respondents with the following hypothetical situations and questions (see below). We used absolute values in euros presented either as purchase prices for past purchasing or financing customers or as monthly leasing rates for past leasing customers. The euro values were derived from previous questions in which respondents indicated how much they spent on their last car purchase (or leasing contract).

Situation 1:

You want to buy a new car. A car dealer in your area offers exactly the model you want. The following information is displayed on the sales sign: Manufacturer's suggested retail price: €55,000, dealer's offer price: €50,000 (example values).

Question 1.1 (best possible price):

Assuming you want to negotiate the price, what is the best possible final purchase price you think you can negotiate the dealer down to (in €)?

Question 1.2 (probability of best possible price):

How likely do you think it is that you can successfully negotiate this final purchase price (in %)?

Situation 2:

Another, very similar car dealer offers exactly the same model that you want to buy. This dealer offers the car at a lower price. The price here is fixed and non-negotiable. Both dealers are the same distance from you, but you can only visit one of them. Dealer A's offer price: €50,000 (price negotiation possible), Dealer B's offer price: €48,500 (no price negotiation, fixed price) (example values).

Question 2.1 (fixed price alternative):

Do you decide to go to Dealer A and try to negotiate the price or buy the car from Dealer B at the fixed price?

We repeatedly asked respondents Question 2.1 and with each iteration of the question we gradually reduced the fixed price of Dealer B until the respondent finally decided in favor of the fixed price and thus against price negotiations. On average, a respondent was presented with 6 different price scenarios.

Source: Customer survey October-November 2022, N = 510 (recent new car customers from Germany).