The rationale behind attempts of MG Rover to forge alliances

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This essay explores the rationale behind MG-Rover’s attempt to forge alliances. It begins with a brief history of the brand because in order to understand the rationale for alliances, you must understand where the company found itself at the start of the new millennium.

The Rover brand emerged over a century ago and provided high-quality cars to the middle-classes. Rover was then assimilated into the nationalized British Leyland in the mid-1960s. However this was, in hindsight, seen as a failure as it starved the brand of investment and seriously harmed its reputation for quality. In 1982, the Austin Rover Group was spun-off and a recent strategic alliance with Honda was giving them access to Honda's engineering expertise and produced some excellent results. However the group was then sold to British Aerospace in 1988 who in turn sold it on to BMW in 1994. This ended the alliance with Honda.

Within a year, Rover was, within BMW circles called "the English patient" as they believed they had bought a chronically sick car company. The production and labor facilities were seen as antiquated and the model range in urgent need of updating. BMW persevered and invested billions of pounds in revamping the whole operation to try to modernize it. They finally gave up in 2000 when the drain on BMW's resources was threatening their own strong balance sheet. The company was sold to a group of private investors, the Phoenix Consortium, for a nominal sum. This newly formed entity was named the MG-Rover group. This group had, however, lost two key niche brands along the way - the Mini and the Land Rover. MG-Rover had, in effect, been picked clean of key satellite brands and what was left was a company with essentially three models; the Rover 25, 45 and 75. The very problems it faced at this juncture were the reasons it attempted to forge alliances over the next five years with other firms including Proton, Tata, China Brilliance and SCIA. These reasons included:

**Lack of production volume**

MG-Rover lacked any serious production capacity. The top five car producers all manufactured over three million units a year each in 2003. In comparison, MG-Rover’s production of 107,000 units in 2003 was almost derisory. The key to success in the automobile industry is either volume or a successful niche product. With volume, you get economies of scale which can carry the high costs of developing a new model. MG-Rover's 107,000 cars alone could not justify carrying all the overhead necessary to justify new models. Without new models, sales fell. The attempt to forge an alliance was an attempt to escape from this vicious circle. The attempted collaboration with Chinese firms was an attempt to rapidly scale up production in a single market with huge potential. Equally the Chinese were eager to acquire a 'Western' brand and technology.

**Lack of R&D Capacity**

When BMW sold the Land-Rover brand to Ford, the Research and Development facility at Gaydon also went with it. This deprived Rover of most of its R&D capability which is vital in today's car market where
constant innovation is the key to success. Combined with its lack of production volume, MG-Rover lacked any ability to perform serious innovate research itself. The joint ventures with Honda and BMW had shown what MG-Rover was capable of but without deep-pockets it was stuck in a time-warp.

**Poor Model Range**

This is obviously linked to the lack of R&D but exposes even deeper strategic problems within MG Rover. Even when BMW owned Rover, the only new model it launched was the Rover 75 - an executive saloon. Yet the growing segments in the market were the super mini, the Sports Utility Vehicle and the MPV. MG-Rover had little or nothing in these segments. Ironically MG-Rover had, under BMW, drastically improved its quality of the range it had. However, the result of this model gap, was that it was hemorrhaging market share in its only real market; the UK. In 1990, it had 13.62% of market share in the UK, by 2004 it was down to 2.99% - see graph below. MG-Rover simply did not have the full range of models to keep attracting younger customers. An alliance was needed to flesh out their model range. In hindsight, now it can be seen that the strategic alliance with Honda was probably Rover's best chance of success. It allowed Honda easy access to the UK market and Rover would have gotten access to their R&D and a wider product range. They had jointly developed five models before the break-up of their alliance. It is clear that Rover was probably seeking what it already had had with Honda. Graph from p.17 'Who Killed MG Rover': A special Report from Cambridge MIT Institute's Centre for Competitiveness and Innovation: Trumpington St., Cambridge, UK

**Lack of International Markets**

MG-Rover was essentially an English company. The only internationally recognizable brands it possessed were Mini and Land Rover. When these were gone, it was tied to the vagaries of the UK economy and could never achieve the global economies of scale that, for example, Toyota or VW had. This weakness repeatedly hindered Rover over its history. Because when it did have good models like the Montego, Maestro and Metro, it simply did not have the distribution network to sell them internationally to gain volume and higher marginal profits.

The alliance with BMW gave it a renewed potential for accessing the European market and beyond but when BMW was gone, Rover was back to square one. It needed alliances to rectify this and help it to expand geographically. However, established world markets were oversupplied and the only real place it could turn was developing markets. Rover still had the technological experience which was marketable in these regions - this is why China drew their interest. China had the mass market that would allow it to scale up production in a low labor cost economy - it seemed an ideal solution to Rover’s problems.

**Negative Publicity**

It is worth noting that the weaker MG-Rover became, the lower its sales went. The public did not want to buy a brand that might not exist next year. A successful alliance may well have stemmed this effect and even turned it. MG-Rover needed the imprimatur of another successful company. The only period when their image was really improving was when BMW owned it and its prestige and technology rubbed off - but even this was not enough to support sales.
Lack of Cash

This real issue at the core of MG-Rover's problems from the moment it broke from BMW was cash. Without rich parent pumping money into the company, it was consuming its own capital to cover the day to day losses it was making. By 2003, it had even sold its main production plant, Longbridge for 45 Million pounds and was leasing it back. In 2001, it had sought investment from China Brilliance in order to fund new models but this deal eventually fell through. Again in 2004, Rover and the Shanghai Automotive Industry Corporation (SAIC) were courting but the consummation never took place. SAIC was just not willing to pour in the cash necessary. Their logic was incredibly sound - if BMW cash and technology could not turn Rover around, could anyone do it? The Chinese also realized that they knew more about their own markets than Rover did and all they were really after were Rover's models and technology; not a potential money-pit. In the end, all that was bought - by the Nanjing Group - was the rights to the MG-Rover's models and technology for 67 Million pounds. Later the Longbridge plant was physically stripped of the machinery and this was shipped to China.

It must be asked if the real rationale for a search for alliances may really have been a quest for someone to finally buy any value that was left within MG-Rover. The men behind the Phoenix Trust were not new to the industry; they must have known the situation MG-Rover was in. In the final analysis, when MG-Rover split with BMW it was too big to be a niche market player and too small to be the global player it wanted to be. It needed to forge alliances to rectify these problems. It needed technology, a new model range and a brand boosting connection with another firm. But most of all, it needed cash.

Questions:

1. What are the reasons for MG Rover's diseconomies of scale?
2. Explain how innovation and a good research and development capacity could have saved MG Rover.