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## Case 12: European Motorcycles

### BACKGROUND

**Firm:** Bain  
**Round:** 2006 FT, Final  
**Content:** Qualitative and quantitative

### CASE TOPIC

Our client is a private equity firm that has just purchased a motorcycle manufacturer based in Germany that makes sporty bikes. Currently they supply motorcycles to Europe but have no presence in the US. They are looking to expand the business into the US but are unsure of how to do this. They are considering two models: one is selling through existing dealerships in the US, the other is building a flagship dealership and selling that way.

Our client wants to consider a few issues. First, is this expansion a good idea? Second, which model would be the best to pursue?

As a starting point, tell me a little about the high level pros and cons of building a flagship dealership versus selling through existing channels.

### INTERVIEWER BRIEFING

#### **Recommended Approach:**

High level, you're going to need to hit the numbers right when they're presented and be able to step back and synthesize into some sort of meaningful recommendation. Interviewer should keep asking the interviewee to summarize and back-up assumptions.

Interviewee should keep in mind that this is a PE shop and wants to flip the company quickly – this is a common theme through Bain cases.

#### **Key Facts:**

##### Flagship:

*Retail Price: \$20K*

*Cost: \$10K*

*Cost to set up flagship: \$3 million*

##### Existing Channel:

*\$250K start up cost*

*Retail Price: \$20K*

*Distributors require 33% gross margin, then there will be a 3% allowance of the sales price that will be reserved for return, selling costs, etc.*



## **EXAMPLE DIALOGUE**

**Interviewee:** I would think that opening a flagship dealership would have a lot of pros. First, it would probably allow for higher margins as you would own the distribution. Second, you could train the sales people to sell the right way, position the product correctly, etc. You would also then control your customer data, ability to control marketing messages in the dealership, etc. On the downside, there is the capital investment, the fact that existing dealerships have relationships with customers already in place, distribution channels already in place, and local market knowledge. Your brand name is also not well-known in the States, so opening a flagship dealership might be difficult.

**Interviewer:** *OK, that makes sense. What would you think about the profitability?*

**Interviewee:** I would assume that owning your own dealership would be more profitable in the long run, but short term it might be better to go with the existing channels b/c of the capital investment. Given that this is a PE firm, they probably don't want to invest a ton of capital or hold for too long.

**Interviewer:** *That sounds good – let me give you some numbers and let's see if they match your hypothesis:*

**Flagship:**

*Retail Price: \$20K*

*Cost: \$10K*

*Cost to set up flagship: \$3 million*

**Existing Channel:**

*\$250K start up cost*

*Retail Price: \$20K*

*Distributors require 33% gross margin, then there will be a 3% allowance of the sales price that will be reserved for return, selling costs, etc.*

**Interviewer:** *What's the breakeven in both cases?*

**Interviewee:** The breakeven in terms of a flagship store is 300 bikes ( $\$3,000K / [\$20K - 10K]$ ). For the distributor model, you assume a 33% gross margin, so 33% of 20K is 6.6K. That means we still get 13.3K. With a 3% allowance, that means we roughly take in 13K for every bike. That's 3K profit.  $\$250 / \$3$  is about 83 bikes.

**Interviewer:** *Right. What does that tell you?*

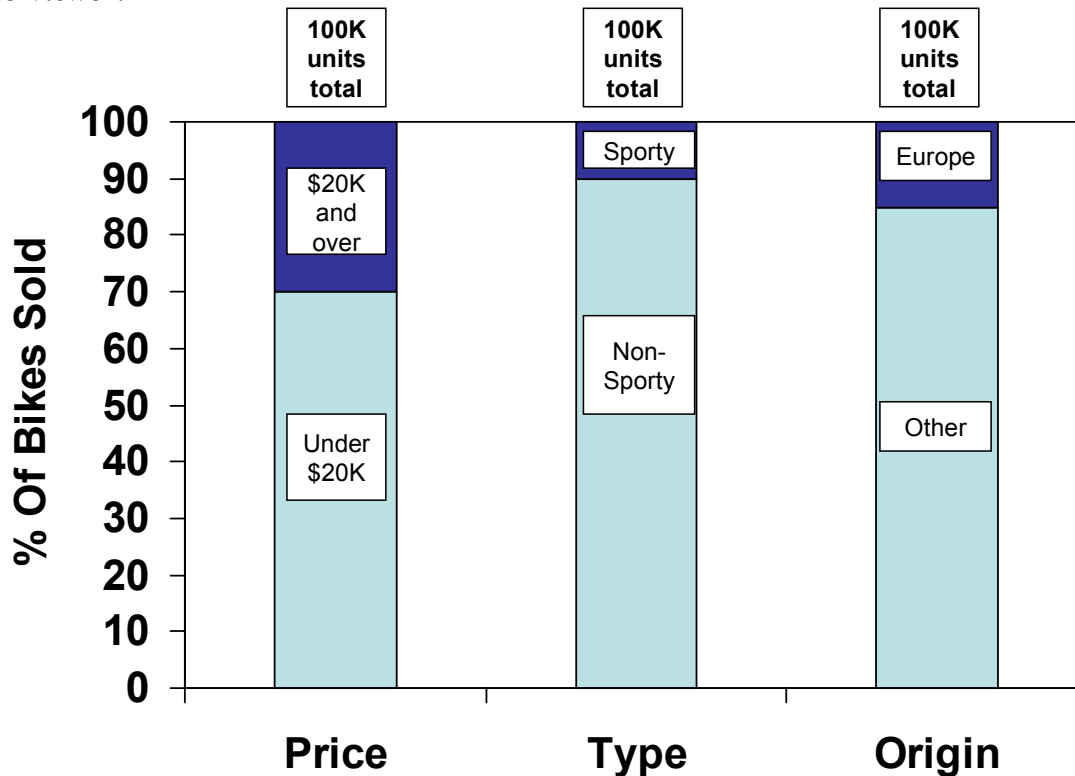
**Interviewee:** That our breakeven is lower in the existing distributor model. It also tells me that in terms of investing in the long term the flagship would be MUCH more profitable.



**Interviewer:** So how conceivable are these numbers?

**Interviewee:** I would think selling 83 bikes should be fairly easy in a year. 300... it also sounds reasonable.

**Interviewer:**



(Presents chart – chart shows all sorts of things but relevant info is that 100K bikes are sold in the US every year, and it’s broken down 3 ways. First by country of origin, next by price, third by type. Turns out 15% of bikes are from Europe, 30% are high end (20K or higher), and roughly 10% are sporty.)

Now what do you think?

**Interviewee:** (takes time to think) Alright, so now I know 100K bikes are sold. So 15K of them come from Europe, 30% of those or 4.5K are high end, and 10% of those are sporty. That’s 450 bikes. So maybe 300 would be a stretch, and 83 might even be tough if there are strong competitors.

**Interviewer:** I would argue that the country of origin doesn’t matter. A sporty 20K bike is a sporty 20K bike, right?

**Interviewee:** I’d actually disagree. Think about automobiles – some people buy German cars b/c they want to buy German cars, nothing else. Or think about beers. Some people only like



Belgian beers for no reason except that their Belgian – it's an image thing, right? (Note: This was not well received by the interviewer.)

**Interviewer:** *OK, there's no right or wrong answer. Assume that I'm right and the market is much bigger. Now what?*

**Interviewee:** OK, then it seems feasible. So short term the better play is to use distribution centers that are already in place, but long term it would be to build a flagship.

**Interviewer:** *And does the fact that it's a PE client have any bearing here?*

**Interviewee:** Well, they'll want to turn it over quickly and not pour cash into it, so they'd likely go with existing channels and not build. They also might want to examine why they're thinking about the US – maybe they can grow in other parts of Europe more efficiently and profitably.

**Interviewer:** *Great.*