Chapter 10

SERVICE PARTS MANAGEMENT IN CHINA

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**Abstract:** Aftermarket service parts can be an extremely lucrative business, yet most OEMs only capture a fraction of its profit potential. The situation is even more pronounced in China and other emerging markets, where cultural behavior, infrastructure limitations and market barriers make it hard for foreign OEMs and their dealers to compete with unauthorized service parts providers. This chapter examines the unique challenges of selling and distributing service parts in an emerging market, and offers foreign OEMs specific advice to make their service parts operations more efficient and profitable.

### 10.1. Introduction

The service parts business is critical to the success of any manufacturing company. It keeps customers happy by providing them with replacement parts they need to keep their equipment up and running. And in mature markets, it is typically a source of enormous profitability. Yet many manufacturers take their service parts business for granted, leaving a lot of potential profits on the table.

Emerging markets are a different story altogether. Customers in developing countries tend to be less sophisticated than their counterparts in mature markets and don’t place as much value on service parts. They tend to run equipment until it breaks, then seek out the cheapest possible replacement, often purchasing substandard parts from questionable sources, or fabricating copies themselves.
Under those conditions, it can be difficult for foreign manufacturers and their dealers to command a premium price for genuine OEM service parts — pushing many aftermarket businesses into the red.

In this chapter, we examine the unique challenges of operating an aftermarket business in an emerging economy and explain why it’s worth doing well. We look at the differences between a service parts operation and a traditional production-oriented supply chain. We describe the logistical challenges and other factors that make it hard for foreign OEMs to be efficient, price-competitive and profitable. And we offer specific suggestions to help companies improve the financial performance and competitive position of their service parts business. Our primary focus is on China — the world’s preeminent emerging market — with real-world examples from leading global manufacturers. However, our insights and recommendations are for the most part applicable to any company in any emerging economy.

10.2. Why Worry About Service Parts?

In mature markets, the service parts business is generally very profitable. Yet few companies even come close to tapping its full potential. According to common wisdom, customers will always need to buy service parts; therefore the aftermarket business can basically run itself. And since most service parts operations are already profitable — at least in mature markets — it’s hard to argue the point. The problem with that hands-off approach is it creates a safe harbor for inefficiency and overlooks valuable growth opportunities, leaving a lot of money sitting on the table.

Emerging markets present a greater financial challenge for service parts, but are still worthy of attention for two reasons.

- **Customer satisfaction.** In the short term, service parts are a key driver of customer satisfaction — even for customers who don’t realize it. High quality parts reduce unplanned downtime, extend the useful life of equipment, improve operating safety and maximize resale value — helping a foreign OEM establish a reputation for quality and reliability, while building a base of loyal customers. Service parts can also be a significant source of incremental revenue and profit.

- **Long-term profitability.** Emerging markets like China eventually develop into mature markets with tremendous profit potential. Focusing on service parts now positions an OEM to dominate later, when the stakes are much higher.