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Exam-style question

Mass and niche markets

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Check your answer to the question on pp. 2–3 of the magazine. This question relates to the AQA specification.

Sample answer

One benefit of having a niche market product for Rolls-Royce is that it can tailor-make its cars to meet the specific needs of individual customers. For example, a Silver Dawn can be built with different types and colours of leather upholstery. This level of customisation creates a unique selling point for Rolls-Royce and higher levels of customer satisfaction. Consequently, customers are more likely to pay the premium prices for the Silver Dawn, allowing Rolls-Royce to achieve higher profit margins than would be possible on mass market cars such as a Ford Mondeo.

However, as such levels of customisation mean Rolls-Royce is unlikely to benefit from economies of scale in the purchase of bespoke leather, the price of raw materials is likely to be significantly higher for each car made. This means the margins of safety per car sold need to be set higher as a percentage than mass market cars, meaning that Rolls-Royce risks being unable to break even if it misses selling even a small number of cars compared to its sales forecast.

Another benefit to Rolls Royce is that even though volumes of sales are much lower than mass market cars the level of growth in sales can be significantly higher. In 2022 Rolls-Royce reported sales of 6,021, which represents a rise of 8% over the previous year, compared to mass market manufacturer Toyota sales rising by just 6.13% for the same period. Rolls-Royce profit margins are allegedly about 40% on each car, while Toyota's margins are approximately 6.61% (Macrotrends 2023). Therefore, niche market sales are over six times as profitable than mass market cars. Consequently, Rolls-Royce's profit margins translate into significant overall profits because other costs such as marketing, production facilities and staffing can be kept low due to the small volumes of production. This leads to more of the profits on each vehicle translating into profits for the company.

However, Rolls-Royce may not benefit from many economies of scale that mass market producers such as Toyota or Tesla can benefit from. For example, Tesla's use of technical economies of scale in their use of the Giga Press allows them to cut down from 40 to 2 parts for the pressing of the Model Y body. This allows the unit costs of cars to decrease significantly while maintaining high levels of quality compared to Rolls-Royce, who are unable to afford the US\$108 million for each Giga Press. This may allow Tesla and other mass-market manufacturers to have much lower quality and reliability issues with each car in the medium-to-long term, with Rolls-Royce possibly being less reliable and prone to faults. This could mean that even though initial profit margins are higher this could be significantly reduced by returns from customers for warranty claims as well as having a negative impact on brand image.

In conclusion, niche market production of cars by Rolls-Royce allows for the bespoke production of each individual car, which adds to the usp and brand image of the business. Due to the likelihood that Rolls-Royce combine niche market with job production, they have benefited from using this to add value to their cars, resulting in being able to offer individualised features such as works of art in the dashboard. This allows the business to substantially increase its profit margins. However, the risk of this approach is that, due to the relatively small volumes sold, the business may not be able to compete with the increase in quality of panel fit that mass producers such as Toyota are able to gain through the use of robots and specialised equipment, meaning Rolls-Royce may actually lose customer satisfaction in the medium-to-long term as the product does not meet expectations. However, as Rolls-Royce has been owned by BMW since 2003, they are likely to be able to benefit from the benefits of mass-market savings, such as cheaper unit costs for engines, while at the same time being able to produce bespoke cars for their luxury clientele, converting an even greater proportion of their profit margins to net profits.

Sample examiner comment

Mark: 16/16 (Level 4 — an excellent response fully focused on the question)

A thorough knowledge and understanding are shown of the benefits Rolls-Royce being a niche market product.

Application is shown through the use of appropriate context applied to the question.

Coherent and logical analysis is linked together, looking at the relevant importance of internal and external causes of business failure to a range of business situation, using context-based quantitative and qualitative data for competing arguments.

An evaluation of competing arguments with context is used to support a judgement about the relative benefits of niche market products to Rolls-Royce.

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