The significance of investment in zipcar business essay

Zipcar is a viable business and represents a significant investment opportunity. The business model has been proven in Europe. Zipcar have made technological enhancements such as online reservation systems and wireless access control which improve on the existing European business model. These enhancements streamline processes, minimize required assets and working capital; and increase accessibility of the service. The advantages given by this technology will be short lived, since one can expect them to be copied. The management team must implement a rapid growth strategy to capture the market and prove this breakthrough concept. They will need to innovate continually and expand into new markets to maintain that position.

The business model was first proven in Europe and is best suited to dense urban areas. The launch of Zipcar coincides with increased willingness amongst its principle US customers (“ college-educated urban dwellers”) to use its service. Amongst this segment of the population maintaining a car is becoming less of a status symbol and increasingly less economical for those who drive less than 6000 miles a year. For this group demand for “ short term, on-demand private car access” and an increased awareness of the environmental damage created by automobiles are fundamentals which support the Zipcar model.

Although similar services existed in Europe, the North America market is relatively uncontested. In both Europe and North America an easy to use, convenient solution which didn’t require large overheads was absent. The technological advancements made by Zipcar deliver a quality service with low working capital requirements.

In Europe some consolidation had been taking place among competitors. The car sharing market had been growing at 30% annually with very little investment in advertising. This demonstrates the market appetite for the service. The industry was estimated to be worth $200m in Europe. Previous North American competitors had focussed on the environmental impact of the service rather than convenience and cost effectiveness. Zipcar emphasises both and thus meets more effectively societal needs. Once customers are familiar with the process of using Zipcar's service the majority will continue to use the service due to convenience and cost savings. As a result there will be fewer cars on the road and the environment would benefit.

Zipcar's revenue growth is particularly strong over the first two years of operations. The first four years represent strong revenue growth. It is crucial for the management team to have identified alternative sources of revenue during this period to secure the future direction of the business. A seasoned management team with experience of automotive is crucial for the long term success of Zipcar.

Gross margins are strong and reflect the fact that as Zipcar's customer base grows, Zipcar are able to leverage fixed assets more effectively. Both gross and Net margins are in excess of what would be considered fair (40% and 15% respectively) in an investment of this type.

Year 1

Year 2

Year 3

Year 4

Year 5

Revenue

355, 388

1, 026, 429

1, 385, 193

1, 644, 483

1, 864, 520

% Revenue Growth

189%

35%

19%

13%

Costs

180, 975

215, 532

233, 956

236, 400

237, 952

Margin

49%

79%

83%

86%

87%

Assuming a valuation of 4 x Year 5 EBIT. After five years Zipcar would be worth $1. 9m. Robin Chase was looking to raise $1m. This represents a return 90% over 5 years, ignoring dividends. The following table estimates possible valuations of the company based on EBIT. Assuming an investment of $1m, returns in excess of 20% can be achieved by exiting the investment from year 3.

Year 1

Year 2

Year 3

Year 4

Year 5

EBIT

(36, 007)

185, 933

300, 463

401, 097

480, 614

EBIT x 4

743, 732

1, 201, 852

1, 604, 388

1, 922, 456

The biggest potential competitor is from car rental agencies and manufacturers. Volkswagen could thus be a collaborator, competitor or both. Car manufacturers are a potential collaborator, they have a vested interest in helping to test Zipcar's success. Volkswagen estimates that in 2007 there would be 2. 45m shared vehicles in EU. Auto manufacturers are likely to emulate the business model once proven.

The government is key a collaborator. Zipcar should court the public sector as a keystone client. By building close relationships with the public sector, Zipcar could realise secondary benefits: subsidised parking, access to public sector workers but most importantly an opportunity to be close to government and to refine their strategy as new regulation is introduced. Environmental regulations are likely to increase the costs of car ownership and redirect customers to alternatives like Zipcar.

Technological factors which coalesce to support Zipcar, include the advent of wireless technologies – which support the tracking and use of assets, and continued adoption of the Internet, for the purposes of reservations and to communicate with customers.

Robin Chase's suitable as a leader

Whilst Chase had the qualities to bring the Zipcar business into existence and help it to survive, the business required the expertise from someone used to bringing businesses to scale. Chase successfully saw the demand for Zipcar and established the organisation to support her vision. With limited angel investments she has successfully managed prove the concept and garner resources in support of the business. By continually analysing the usage data she is able to adjust the business model as needed to ensure viability. However, Chase is not the best person to take the business to scale. As investors observed both Chase and Danielson lacked experience in running complex operations and had no previous automobile leasing experience.

Chase realised that she needed support and recruited a short-lived president into the company. She showed her decisive leadership ability when she realised the man appointed to president was not suitable and she acted speedily to remove him. Chase should not be deterred by this failure. A credible management team is required if Zipcar was to be a success and chase is the correct person to structure that team, if not lead it.

Chase should utilise her resolve to exit Danielson completely from Zipcar. Danielson has not demonstrated commitment to Zipcar nor leveraged her relationships with Ford significantly. Chase should come to an agreement with Danielson regarding her share in the business. It is disappointing to note that Danielson’s contacts and experience in the automotive sector where not enough to accurately forecast the costs of the cars when adjusted for credit risks.

Chase should appoint a strong management team with experience of automotive leasing, wireless technologies and operations. This will satisfy investors and provide the right mix of skills to drive rapid growth. Chase is able to establish such a team, her network of advisors is strong. However, she is not the best person to lead the team. After the initial technological innovation, scaling Zipcar’s business will depend as much on operational efficiencies as innovation. Chase has demonstrated that she can innovate, but she should leverage someone else’s skills to operate. She should maintain an advisory interest in Zipcar, in the long term her innovation may support future periods of growth.

Evaluation of the business model

The fundamentals of Chase’s business model in Boston are sound. Boston like many European cities is pedestrian friendly, there are parking restrictions, which would increase the Zipcar’s convenience and although there is a strong public transportation system there are ad hoc times when for many city residents a car would be useful. Chase sized the Boston market at 15, 000 people

The Zipcar business model has the potential to affect all six levels of customer utility. Customer productivity is increased since customers do not have to maintain vehicles of their own. Simplicity is achieved through the online reservation process. Convenience, since cars are located at convenient locations. Confidence in Zipcar will grow as users find that the system works. The Zipcar image and its chosen vehicles convey a fun image. There is societal value in there being fewer cars on the road and thereby a reduction in emissions.

Overheads and managing COGS is a crucial component in insuring Zipcar’s success. A weakness of the model is including the cost of gas in the bundle. Rental car firms operate differently, with empty to empty or full to full policies practiced. Perhaps however, Zipcar do not foresee the affect of high gas prices on margins or perhaps the strategy is that high gas prices would encourage greater use of the service. However, once market share is gained to become profitable it is likely that the model would have to be refined to account for gas and other variable costs. Her desire to stay under the $45 per day threshold was a good strategy (but this cost comparison is misleading as rental agencies do not include gas). However, since Zipcar provides the same form, function and objective as a rental car and since it is a breakthrough service, it is advisable to pitch below this threshold.

Chase’s plan was to launch in a single market and expand in 14 cities in the US. These markets would have to be penetrated quickly to build scale and avoid being copied. Europe had proven that this model was prone to be copied and Chase would have to move quickly to capture the US market, especially given the strength of rental agencies and car manufacturers.

The September data shows that Zipcar has the potential to be more successful than anticipated. At the end of September there were 239 members, whilst the forecasted ended number for year 1 was 440. Customer attrition was also less than expected (3% versus 15%). It is thus crucial that the wireless technology supporting operations be implemented as soon as possible.

Chase’s belief that cars would be parked close to transit stations turned out to be more expensive than expected. Chase had expected the parking would be free. Previously, she revised her original business plan to reduce the upfront fee and increase the hourly rate. This should be revised again to reflect September usage data.

The Zipcar technology covering reservation, access control, billing and parking, communication to and from the vehicle to facilitate management of the fleet is unique and a competitive advantage. This advantage keeps overheads low and allows Zipcar to challenge existing players.

Through high asset utilisation I would expect Zipcar to outperform traditional car rental agencies in income generated by each vehicle. In traditional rental agency revenue per vehicle is typically between $10k and $12k per year.

Year 1

Year 2

Year 3

Year 4

Year 5

Revenue

355, 388

1, 026, 429

1, 385, 193

1, 644, 483

1, 864, 520

Avg. no. vehicles

12

36

49

58

66

Rev/vehicle

29, 615. 67

28, 511. 92

28, 269. 24

28, 353. 16

28, 250. 30

It was right to focus initial investment on the wireless technology platform. This wireless platform will ultimately be the foundation on which the business would scale.

Although Chase's model is not perfect it is credible. Providing costs (gas, insurance and parking) can be kept to a minimum. Or if the inclusion of fuel is seen as a strategy to capture the market, there must be a long term acceptance of the need to change the model once maturity is reached.

The model has some weakness that should be addressed. Zipcar must quickly leverage the technology originally developed in order to maximise utilisation of its assets and to better understand customer usage patterns. The target population is not large enough to sustain Zipcar, other segments should also be targeted. Perhaps, by making alliances along the value chain or with other stakeholders who stand to benefit from Zipcar's success, like the government.

An investors perspective

Zipcar is a disruptive breakthrough player. Its innovative use of technology can capture the market. They will have to take the market quickly before the other big players react. Thus it is crucial to take the business to scale quickly. Zipcar represents a good investment because of its use of innovative and unique technology. This technology keeps overheads and working capital to a minimum. Revenue growth and growth margins are strong, the business has low working capital requirements and returns in excess of 20% will be gained on exit after year 3.

Zipcar’s market must be wider than that of a traditional rental agency. It must focus on residents and not just travellers.

Zipcar requires a management team capable and experienced in extracting the maximum efficiencies in business operations. Zipcar’s success hinges upon selecting the best locations, managing capacity, building strong relationships with stakeholders, and managing the servicing of its vehicles. Zipcar’s management team must be committed, experienced as well as capable. Zipcar is only a viable investment if a suitable team of operations experts can be built. I would provide funding to this venture due to the high return on investment if a suitable management team can be structured.