POWER STEERING

Steering your dealership to higher profits

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June 2020 pre-tax net profits for new vehicle dealers were excellent and possibly the best overall profit month in 40 years. As you observe in the enclose sales and profit results survey for June 2020, the average dealer made a pre-tax profit as a percent of sales exceeding 4.0%. Remember, the average profit margin for new vehicle dealers from 2010 - 2019 was in the 2.3 - 2.5% range. We have never seen such good results in over 40 years. Though dealers' total dollar sales are down slightly from the average month of 2019, profits and profit margins overall are improved. Since vehicle gross profit margins are in the normal range, these higher profits mainly are due to reduced expenses. How long will dealers keep their expenses at these lower levels before they allow them to go up and profits go down?

Monthly Profit Trends

	JUNE BETTER THAN MAY	JUNE WORSE THAN MAY	JUNE BEST PROFIT MONTH	JUNE +3% PROFIT % SALES	JUNE LOSS MONTH	JUNE Y-T-D LOSS
CHRYSLER	85%	15%	85%	65%	0%	15%
FORD	80%	20%	65%	65%	5%	15%
G.M.	90%	10%	85%	55%	0%	20%
IMPORTS	90%	10%	80%	80%	0%	20%
OVERALL	85%	15%	80%	70%	0%	15%

Email

We still see many dealers where their employees use their personal email address to conduct dealership business. Some dealers do not supply each employee with their own dealership email address. For some employees, they prefer to use their personal email address for dealer business. You need to supply to each employee their own dealership email address and require them to use this dealership email address. The Iowa Automobile Dealer's Association recently covered this email issue in their dealer newsletter.

"Setting goals is the first step in turning the invisible into the visible."
Tony Robbins

Inside

Factory Relations

We were recently involved with an existing new vehicle dealer that tried to purchase the same manufacturer's other franchises. This dealer was turned down on the purchase of these two franchises. The factory reported excuse was the buying dealer was new vehicle sales ineffective. This smaller dealer was below the 100% guideline by approximately 40 units per year. This dealer had been trying for 2-3 years to obtain and keep a larger reasonable inventory day's supply, but was ignored by this manufacturer. This is why all dealers need to try and keep their new vehicle sales effectiveness at least 90% or better. Even if the factory does not supply adequate inventory, email your factory about this at least monthly, and at times the factory has a "corrupt" scoring system, but keep trying. Also, since the 2 lost franchises now will be without a dealer representing those franchises in this market area, this factory will annually be losing incremental new vehicle sales. This indicates the "ignorance" of this factory.

We had an import dealer being given a 85% new vehicle sales effectiveness score where it appears below 90%, though not good, put this dealer in "jeopardy" with this factory. The dealer complained about its lower day's supply of new vehicles, not its share, and the factory used the excuse that this dealer was always open in this Virus time period, while other same make dealers were "closed." This was not true and a false factory excuse. We analyzed the day's supply for this dealer based on actual numbers compared with all other same franchise dealers where we had their May and June financial statements. This dealer had approximately a 30 day's supply of new vehicle inventory while all the other dealers we had financials for reflected an average day's supply of 55. This would explain why this dealer's sales effectiveness would go down. Not enough new inventory compared with other same make franchises. It was not the dealer's fault, but the factory intentionally or unintentionally (poor allocation) not supplying a comparable day's supply of new vehicle inventory. When you see this happen, you need to respond in writing so you are not "penalized" in the future by your factory.

Future Profits

With current profits so good, last three months (May, June, July) what do dealers need to do and not do to maintain these higher pre-tax profits? We see higher pre-tax profits for the last three months even though new unit sales and used retail sales seem to be slightly reduced. Parts and service sales also seem to be down slightly. In order to maintain these higher profits, you should keep new inventory slightly above the current low levels and let your expenses remain where they are. We expect dealers will hire back some employees and increase new inventory materially along with increasing other expenses including advertising. We ask why allow any of these changes to take place rather just keep the inventory, excluding used, level and expense levels where they have been during the last three months. Sometimes dealers become "greedy" by thinking increasing advertising will sell more and increase profits. Doubtful. Try to keep staffing and expenses where they have been over the last three months.

Rent and Equivalent

We are often asked about rent and rent and equivalent and what is reasonable. The NADA publishes in its monthly AVERAGE DEALERSHIP PROFILE a metric: RENT & EQUIVALENT as a percentage of gross profit. Rent & Equivalent generally includes: rent, amortization of leasehold improvements, depreciation of building, mortgage interest, facility insurance, utilities, property taxes and facility maintenance. The NADA metric for last year was 10.9% of total gross and $906 per new vehicle retailed.

We recently took a sample of our dealers and had these metrics: Rent & Equivalent of 9% of gross profit and rent only made up 65% of Rent & Equivalent. The average rent was approximately $348,000. If the average dealer in this sample charged 8%, common rent factor as a percentage of facility fair market value, the average fair market value of the facility would be $4,350,000 ($348,000/8% = $4,350,000). This might give you an idea of "reasonable" rent for your dealership if you are the landlord and when negotiating with your unrelated landlord.

Used Vehicle Inventory

As we all know, there is a shortage of used vehicle inventory right now. This makes the current real world values very volatile and "speculative." We have seen values for some vehicles vary by several thousand dollars compared with third party guides. This should balance out based on our experience once the new vehicle sales and inventory catch up with public demand so dealers have a reasonable amount of used vehicle trade-ins in inventory. This might happen by the spring of 2021. We have seen instances where the number of used vehicles over 16 year's old approximates 25%. This seems high and could be an indicator of increased used retail sales. This probably indicates used vehicle business will improve and used prices will remain steady or go up compared to the last year or two.

Cash

We regularly look at dealer monthly financial statements and observe large cash balances. Often, the office is "slow" and does not pay off and/or pay down new and used floor plan on a daily basis when the dealership has a large amount of cash. You might have your office show you the page from your monthly bank statement that reflects the daily cash balance. If the balance is always well into the 6 figure balance or higher, you might have the office pay down, not pay off, the floor plan balance on some vehicles to say $1,000. We still like the "free" inventory service of the floor plan lender "touching" the floor planned vehicles. This reduction will save you some interest expense now and it will be a good habit to get into when floor plan interest rates go up.

SBA - PPP Loan Program

With the law changing on this program, it will be to the advantage of most dealers to compute their forgiveness for the eight week period and if under 100% then use the new 24 week program. Most likely the 24 week alternative will yield a higher forgiveness amount. Also, dealers have several months to complete their loan forgiveness application with their lending bank. We still feel dealers should not make an entry to put any of these "loan" amounts into income. As of today, most do not know for sure how much is forgiven and why book any of this into income to distort their dealership monthly profits? Wait until you know what the actual amount is, or have your CPA put the forgiven amounts into income on the income tax return.

We like the monthly financial statements to show the "real" profit picture for reality purposes and for comparative purposes.

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