POWER STEERING

Steering your dealership to higher profits

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June 2015 was an improved profit month for 60% of new vehicle dealers compared to May 2015. As you can see below in the Monthly Profit Trend Analysis, 30% of new vehicle dealerships made 3.0% pre-tax net profit on sales in June. The baseline would approximate 2.5% of new vehicle dealerships averaging a pre-tax return on sales year-to-date as reported by the National Automobile Dealers Association (NADA). 20% of dealerships had their best month of the year and very few dealers, 5% or less, are in a loss position for the year.

June Profit Trends

	JUNE BETTER THAN MAY	JUNE WORSE THAN MAY	JUNE BEST MONTH	JUNE 3.0% OR BETTER PROFIT % SALES	JUNE Y-T-D LOSS
CHRYSLER	75%	25%	35%	10%	0%
FORD	60%	40%	25%	30%	5%
G.M.	45%	55%	15%	30%	10%
IMPORTS	60%	40%	15%	35%	10%
OVERALL	60%	40%	20%	30%	5%

Nationwide, as reported by the *Automotive News*, June 2015 new vehicle sales were down from May 2015, but June 2015 was improved over June 2014. July 2015 new vehicle sales were improved over June 2015, and better than prior Julys for several years.

Pre-Tax Net Profit Effectiveness

The enclosed survey reflects June year-to-date pre-tax net profit as a percentage of sales and pre-tax net profit as a percentage of gross profit and other income. As you can see, our group of 200 + dealers reflects 2.3% and 17%. The NADA through May 2015 reflects 2.5% and 19%. If you are well below either of these two metrics, you might analyze why.

"The difference between a successful person and others is not a lack of strength, not a lack of knowledge, but rather a lack of will."
- Vince Lombardi

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Dealership Buy-Sells

From our perspective, there are not that many dealership buy-sells occurring due to dealers making more profits today than in the past and fewer dealers losing money or being forced to sell. One common issue we see is the asking price for Blue Sky compared to the asking price of the real estate, along with the leaseholds paid for and "owned" by the Seller. A general rule for Blue Sky and real estate value is the more one category might be, the less the other category should be. If the amount asked for Blue Sky is high and the amount for the real estate is high, the buyer will recognize that buying the real estate at too high a price will cause the rents to be higher than reasonable which will lower the profits and reduce the computed Blue Sky based on expected profits. Sellers need to recognize this concept and price the real estate value in line with the Blue Sky. At times, we find sellers wanting to obtain the full fair market value for the real estate and sell the unamortized leaseholds-building costs paid for by the dealership. In this situation, the buyer is being charged twice for some portion of the real estate. Some might think this is acceptable. However, this may drive off the more knowledgeable, qualified buyers. In summary, don't try to sell the buyer the real estate and the leasehold-building improvements and then charge for both. Make sure the real estate asking price is reasonable compared to the asking price of the Blue Sky.

Internet Providers - Managing Used Retail Sales Pricing and Inventory

Every month we review dealers' financial statements focusing on various metrics. One main metric used is retail front-end gross profit margins. With the average and median used retail front-end gross profit margin approximating $1,800, we focus on this dealer metric for those that are in the low $1,000 range or less. Most of the time when we call these dealers, we usually find their staff is using an internet provider/pricing service to set the initial asking price for the vehicle. The dealer usually asks us how we know that. We let them know it is a common trait and we usually guess right 80% of the time. We hear from the dealer that their overall used inventory is closer to wholesale value than normal. Some dealers also think they are now selling more used because their prices are lower, but most times they are not. With respect to selling more used vehicles, those in the industry see common trends of the ratio of new retail to used retail. Usually for these dealers, their ratio of new to used does not indicate they are selling a higher percentage of used retail. We often hear from dealers that their used inventory is closer to being on the "money." We then ask them: if you have $300,000 of "water" in your used inventory at the beginning and end of the year and your front-end gross profit margin is $1,800 during the year, what is your real overall used retail front-end gross profit margin for the year? Some dealers answer less than $1,800; some dealers don't know, and some dealers answer $1,800. The answer is $1,800. Though we prefer to have minimal "water" in the used inventory, if you always have $300,000 of "water" and always make $1,800 used front-end gross profit margin, then you are making $1,800. If your staff blindly uses a pricing service and you are making $1,200 or less on used vehicles, you probably need to contact the pricing service to learn how to better use their services and obtain reasonable higher grosses. If they tell you it is OK to have these low grosses, we suggest you have them call us or change vendors.

One Price Selling

We have been in the industry a long time, and we have seen the "one price" selling concept be reactivated several times over the last 40 years. This has included some individual dealerships, dealership groups, large private groups, public auto groups and manufacturers. From our perspective, this concept works well for very few dealers. When we see articles that talk about "one-price," such as Lexus, we think some customers will like this, but those customers that expect an over-allowance on their used trade-in might be displeased and will go and shop at another Lexus dealer. In the past, this concept has been promoted by consultants that are trying to sell their services. This pricing concept is implemented mainly for those customers that say they do not want to negotiate. However, we do not know what percentage of the customers really do not want to negotiate.

Dealer Profit Turnarounds

Some below average profit dealers sometimes hold onto poor performing managers or believe the much lower than average profits are due to something other than the effectiveness of the general manager/general sales manager. We had a few dealerships that either lost money in 2014 or had close to zero in pre-tax profits and made a change in staffing early this year. In three cases, the client hired a new GM/GSM. Within 60 days, these three stores had a material sales and/or profit turnaround. All three of these stores became reasonably profitable with changing this one person and that person either making other staffing changes or making changes in the dealership processes. We see this type of turnaround regularly. If your store is much below average in profit effectiveness, we suggest you give your current lead manager a warning about improving, or start the search for a replacement lead manager. The main two traits these replacement managers seem to possess are intensity and sales skills.

Overtime Changes (Federally Mandated)

As many of you have read, our federal government wants to change the rules and regulations on overtime. In the past, certain dealership employee groups did not have to be paid overtime based on their job classification and as long as they were paid more than $455 per week, or $23,660 a year. The government wants to increase these two amounts to $970 a week, or $50,440 a year. Most dealerships have employees that make less than these amounts and will possibly end up substantially being forced to raise certain employee's compensation, with no increase in results or performance. We have been through this process in the past with federal and state labor department auditors. If you have an employee that will be included in these revised rules that makes both an hourly rate-salary and commission, you do have some options without just giving a large pay increase from new overtime. What we have seen in the past is the hourly rate is reduced, allowing for being required to pay overtime. The hourly rate will be reduced so that after allowing for overtime, the employee will continue to make in total approximately what they made in the past. This needs to be explained to the employee, because when they hear you are reducing their hourly pay, they will not take this well. After you explain to them that after allowing for this overtime pay, they will still make approximately what they previously made, with the same hours worked, and they will eventually understand, but might still be upset for they thought they were obtaining a pay increase. In other ways, there are alternatives to adjusting the historical pay plan to compensate the employee for overtime, but still pay them what they were making recently.

Accounting Procedures

Most dealers do not realize this, but each office has several journals they use to enter accounting information. These journals are also called "sources" at times. Examples are a new vehicle sales journal, cash receipts journal, cash disbursement journal, etc. When looking at the general ledger, an accountant can tell where the entries came from by seeing which journal the number came from. There are usually journal names-numbers for most types of sales, expenses, purchase, etc. There is also a general journal used to make corrections. We are finding more and more offices are over-using this journal to enter many documents, not just correcting accounting entries. This makes it harder to determine what is going on and we would consider it as "sloppy." We suggest you have your office only use the general journal for corrections and not use the general journal-sources for entering original source documents. We suggest you share this short article with your office staff and have them implement this procedure in the future.

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