POWER STEERING

Steering your dealership to higher profits

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Written by Carl Woodward **December 2017**

October 2017 reflected downward trending profits for dealers as compared to September 2017. As you can see below, only 45% of new vehicle dealers performed better from a profit perspective in October 2017 than September 2017. More dealers are sustaining losses than earlier this year as can be seen with the below October 2017 loss month reflecting 20% of the dealers losing money. Nationwide October new car and light duty truck unit sales were the second best month of the year and much better than October 2016. Nationwide November 2017 new car and light duty truck unit sales were down from October 2017, but improved over November 2016.

October Profit Trends

	OCTOBER BETTER THAN SEPTEMBER	OCTOBER WORSE THAN SEPTEMBER	OCTOBER BEST MONTH	OCTOBER 3% OR BETTER PROFIT SALES	OCTOBER LOSS MONTH	OCTOBER LOSS Y-T-D
CHRYSLER	30%	70%	0%	0%	20%	10%
FORD	50%	50%	0%	25%	10%	10%
G.M.	40%	60%	5%	10%	20%	10%
IMPORTS	55%	45%	10%	20%	20%	15%
OVERALL	45%	55%	5%	15%	20%	10%

The five most improved major franchises as a percentage of the market through November 2017 were:
Nissan; Toyota; Subaru; Ram; GMC

The five most reduced major franchises as a percentage of the market were:
Jeep; Hyundai; Dodge; Lexus; Chrysler

"Don't let the fear of losing be greater than the excitement of winning."

-- Robert Kiyosaki

Inside

Rent Factor

Many dealers own the real estate used by their dealership operation. Most dealer's real estate is not owned by the dealership entity, but is leased from a related party of the dealer or dealership. Some dealers have decided to have excessively high or low rent for various reasons. With exceptions, the rent, exclusive of property taxes and maintenance, has some industry guidelines which include:

Annual rent being 7-9% of fair market value of the dealership facility. However, if the dealership has paid for a material amount of the facility costs reflected in leasehold improvements, then the total fair market value should be reduced by some percentage of leasehold improvements. Otherwise, the dealership is paying "twice' for some of the facility costs. Also, it could be that the value of the facility is excessive for the size in dollar sales for the dealership operation. This happens when a dealer's facility size and cost is out of line or high for a dealership's volume.

Monthly rent per new vehicle retailed from NADA metrics, is approximately $650 not including property taxes and maintenance.

Other benchmarks are monthly rent being 1% of monthly sales (not including property taxes and maintenance), or

Monthly rent being 8% of gross profit (not including property taxes and maintenance).

As a summary, we suggest the rent paid, where related third parties are involved, is reasonable based on some of the metrics used by the industry.

Checking Accounts

We are seeing and hearing about a "rash" of counterfeit dealership checks being paid by dealers' banks. We are also hearing about counterfeit EFT's being charged against a dealership's checking account. Some of these checks have forged signatures along with the real dealers' check having the name of the payee on the check changed and these checks have been honored for payment. We are hearing mixed answers from these dealers' financial institutions about how the dealership is being held responsible. This includes:

Holding the dealership responsible for these forged or counterfeit items.

Accepting no responsibility for forged checks, counterfeit checks or false EFT's.

Requiring dealers to sign up for the bank's POSITIVE PAY program. This is a program that requires dealers to approve current and future checks and EFT's that are presented for payment on a daily basis. This can be someone in the dealership office daily approving all items presented for payment to the financial institution or providing a list to the financial institution of pre-approved items.

Dealers have several options on how to proceed with the above "thefts:"

Switch from financial institutions that do not accept responsibility.

Use the banks POSITIVE PAY PROGRAM.

Do nothing.

Make sure dealership has insurance coverage for these types of thefts.

Increase insurance coverage.

Do not ignore these concerns.

Advertising

The enclosed survey reflects gross advertising, before advertising credits, as a percentage of total gross profit plus other income. As you can see, the four dealer groups reflect 10% to 11% of gross advertising as a percentage of gross profit and other income. If your dealership is above average on gross advertising, then to justify it, your dealership should be above average in new vehicle sales effectiveness or used retail unit sales as it relates to new retail unit sales.

Recently, we did a study measuring gross advertising expense for the top 50% of pre-tax profit margin dealers. The pre-tax net profit as a percentage of sales for the top 50% was 3.7% versus 2.5% for the average dealer. In that study, we found the above average dealer spent 9% of their gross profit and other income on advertising. The median dealer spent 7%. What does this mean or what can it mean? It means spending an above average amount on advertising does not translate to dealership having above average results.

Dealership Buy-Sells

We are still seeing some activity on the sale of new vehicle dealerships. Based on conversations we have had, it appears we are past the high for the value of goodwill/blue sky. Some dealers are still trying to sell their stores with "silly" high amounts for goodwill/blue sky. Also, with the national volume of some less desirable perception of franchises, franchises not going up or going down, the conventional formula(s) for goodwill/blue sky do not apply to these franchises. Also, the real estate value needs to be appropriate for the size of the dealership. If the real estate value, asking price, is high for the size of the store, then the goodwill/blue sky should be reduced to allow for this.

National Automobile Dealers Association (NADA) Metrics

The NADA has published its AVERAGE DEALERSHIP PROFILE metrics through October 2017.

	2017	2016
Average annualized dollar sales	$60 million	$59 million
Average net profit before tax % Sales	2.5%	2.6%
Advertising expense net of advertising rebates	8.4% total gross	8.6% total gross
Return on Equity (annualized profit / (pre-tax profit + LIFO reserve)	20%	23%

Insurance Coverage

We try to write once a year to remind dealers to review and confirm their insurance coverage in two categories. The coverages we are concerned with are employee theft coverage and "electronic" theft. Employee theft coverage should be a minimum of $500,000 for most dealers. If you are a large dealer or in a dealer group, you should either have $500,000 per store or a $1,000,000 coverage for the group. For "electronic" coverage we mean funds stolen electronically by EFT or through the Internet. The term "electronic" means different things to different people. We would suggest you meet with your garage liability insurance agent to discuss the possible electronic theft possibilities so you have coverage on all of them. We have seen where a dealer thought he had "electronic" theft coverage, someone from Russia obtained a password to his checking account, and had over $100,000 wired to Russia which was never recovered. These coverages are usually reasonably priced for the risk involved.

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