

# POWER

## S T E E R I N G

*Steering your dealership  
to higher profits*

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Consultants to the Automotive Industry

Written by Carl Woodward

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December 2015 and the year 2015 was very good in the car business. Compared to the last five years, our group of over 200 new vehicle dealers had either a profitable year or their best year based on their pre-tax profit margin as a percentage of sales. The enclosed profit and sales survey reflects that our typical dealer, before LIFO adjustments, made a pre-tax profit margin of 2.4% on annual average sales of \$51 million. This compares closely to the NADA report through October 2015, reflecting 2.5% and annualizing the sales of the NADA of approximately \$52 million. We now have had six consecutive years where new vehicle dealers pre-tax net profit as a percentage of sales is in the 2.2% - 2.4% range.

### Dealership Ownership

We encourage older dealers to sell some of their equity ownership of the dealership to either a successful general manager of the dealership or to family. In selling some equity to the successful general manager, we find the dealer will end up with more "money" down the road owning approximately 90% of the dealership, even if profits go down some, than selling out and earning a very small return on safely investing the sale proceeds. In regard to selling/gifting to family members, it depends on whether the family member works for the dealership or would be an inactive owner. If the family member works for the dealership and has ownership, you are possibly minimizing estate taxes down the road and are more likely able to have the family

member approved as a successor dealer without factory requirements. We have seen factories use the death of an owner to pressure the estate and family to do certain things for approval that are not in the interest of the owners of the dealerships. Dealers often do not realize that the percentage ownership of the equity does not have to be the same as the percentage of voting ownership. You can have a dealer own 10% of the dealership equity, but have 100% voting control. They do not have to be the same.

Think about your situation to determine if it might make sense to sell some equity to your successful general manager or gift/sell to family members.

### Cash Payments to Employees

Many dealers have cash payments, Christmas season payments, "spiffs," bonuses, misc. payments to employees, etc. This is not a good policy, but it happens. Unless the cash payment is a reimbursement for an expense, these payments generally should be put on the W-2 of the employee at the time of payment so the employee pays income and payroll taxes on the cash received. We understand minor payments

at the holiday season might not make it to the W-2 and payroll system. However, it is not a good policy to have regular larger amounts paid to employees in cash. Make sure your office staff minimizes cash payments to employees and these minimal cash payments are put on the W-2 income of your employees.

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**"Success in business requires training and discipline and hard work. But if you're not frightened by these things, the opportunities are just as great today as they ever were."**

**- David Rockefeller**

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## **New Vehicle Inventory**

We are seeing dealers with increased day's supply of new vehicle inventory to an excess. This especially includes GM and Chrysler dealers. We did a study/analysis for a GM dealer as of the end of the year. We used a random sample of 29 GM dealers. We took their new car and new truck inventory based on units at the end of 2015 and computed the average month's sale of new car and new trucks for 2015. Based on these numbers and calculations, we computed a new car average day's supply to be 152 and

median day's supply to be 150. Based on these numbers and calculations, we computed a new truck average day's supply to be 113 and median day's supply to be 99. We have been to several GM and Chrysler dealerships in the last 30 days and observed they are or have run out of room to park new vehicle inventory. One Chrysler dealer told me he has quit ordering new vehicles and other dealers have told him the same thing.

*Automotive News* reported on January 1, 2016 that overall car and truck day's supply was 61 days. We believe that due to fleet sales, the *Automotive News* metric causes the *Automotive News* day's supply to be much less than the "real" retail day's supply might truly be. We suspect that the typical dealer's day supply, at least GM and Chrysler and some other franchises, exceed a 100 days based on our survey. It is not a good indicator that many dealers, domestic and import, now have excessive day's supply of new vehicle inventory based on their retail sales. If they allow this day's supply to "creep" upward, at some point in time they will have to stop ordering new vehicles, even though their factory is pressuring them to keep over-ordering.

## **Dealership Electronic Checking Transfer (ACH)**

Most dealerships allow certain third party vendors electronic access to their checking account to be paid. In some cases, this makes sense, but sometimes the dealer does not have a choice. Vendors that are allowed access include governmental agencies for payroll taxes, sales taxes, license and title fees, child support withholding paid to the government, manufacturers, etc. We looked through several dealer's checking accounts for vendors that have access to the automatic electronic transfer of funds from a dealer's checking account. We often see vendors not included in

the above group. Our advice is not to let third parties have electronic access to your checking account. If you have to switch vendors, then switch vendors. We are concerned about getting money back if an inappropriate transfer has been made or a theft has occurred. It is not worth the risk. Have your office staff let you know all the vendors that have electronic access by reviewing the last two months bank statements and let you know who has access to your checking account(s).

## **Brokers**

Dealers are having more and more brokers involved with the sale of new and used vehicles. Our definition of a broker for this article is an entity that inserts itself between the retail customer and the new vehicle dealer to obtain a financial benefit that is generally detrimental to the new vehicle dealer. Some would call these brokers "free riders" or "parasites" (a person who habitually lives at the expense of others). General Motors has just brought out a broker system involving the public buying used vehicles owned by GM. They might now be called a broker based on discussing

their program with several GM dealers. Brokers can include Carfax, Truecar.com, GM, and other third parties. Some dealers are being near-sighted by dealing with brokers to sell incremental sales while possibly hurting themselves long run. We do not understand why dealers allow these brokers access to their confidential I.T. system at all and allow the increase in the number of brokers to continue to grow at the dealer's financial detriment for minimal, if any, short-term benefits.

## **Credit Cards**

In this month's issue, we have an enclosure written by Alice Zyks. She has authored two articles on credit cards. The first article is about the dealers new risk of being stuck for fraudulent credit card activity, a real possibility under certain circumstances. The second article discusses the various costs you incur as a retailer accepting credit cards. Alice is a professional who works in the merchant services arena.

## Gross Profit Metrics

The enclosed survey shows that our typical dealer has annual sales of \$51 million, pre-tax net profit (pre-lifo) as a percentage of sales of 2.4%. We also reflected total gross profit and other income for the year along with departmental gross profit as a percentage of total gross profit and other income. We include other income because it is so large that it approximates 10% of all department's gross profit plus other income. As those in the industry know, most of other income is generated by the new vehicle department and secondarily by the used vehicle department. The percentage of total gross profit and other income by department for all dealers reflects as follows:

New vehicle department	25%	Used vehicle department	30%
Parts department	12%	Service department	18%
Body department	5%	Other income	10%

For your dealership, you can use this survey to look for possible opportunities. As an example, if you see your used gross less than 30%, it might show you an opportunity in the used department. If service is less than other dealers, it could be you are doing a good job on selling new vehicles, or you might need more effort in service, including adding more technicians.

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**Woodward & Associates**  
P.O. Box 1584  
Bloomington, IL 61702  
carlwoodward@cpauto.com  
**For More Information:**  
Call (309) 662-8797  
or Fax (309) 662-9438