POWER STEERING

Steering your dealership to higher profits

A publication of Woodward & Associates
Consultants to the Automotive Industry

Written by Carl Woodward & Scott Woodward **July 2020**

May 2020 pre-tax net profits were materially improved over April 2020 which was expected by many in the industry. Why? April was such a bad profit month with a large percentage of dealers experiencing a loss. This was the first full month with the Virus issue. Dealers and the public got over the worst of this "shock" by the end of April and losses were reduced and profits went up as a result of reduced expenses and restoration of much of the sales levels. As you can see in the enclosed May profit survey and summary below, excluding smaller dealers, few dealers lost money and the average dealer made 2.4% pre-tax profit on May sales and the median dealer made 2.6% pre-tax profit. These two metrics are approximate pre-tax profit margins for new vehicle dealers over the last 9-10 years. The average dealer's sales for the month were \$4.2 million or \$50 million annually which compares to approximately \$60 million annually for last year. In other words, sales are down compared to 2019 but net profit margins are approximately the same. The below metrics include all size dealers.

May Profit Trends

	MAY BETTER THAN APRIL	MAY WORSE THAN APRIL	MAY BEST MONTH	MAY NET 3% + NET SALES	MAY LOSS	MAY YTD LOSS
CHRYSLER	90%	10%	80%	35%	10%	35%
FORD	85%	15%	45%	30%	20%	35%
G.M.	90%	10%	40%	25%	35%	50%
IMPORTS	85%	15%	30%	20%	25%	40%
OVERALL	85%	15%	40%	25%	25%	40%

"You only have to do a few things right in your life so long as you don't do too many things wrong." – Warren Buffett

Inside

Dealer Information Technology (I.T.)

One of our associates drives a 3 year old used vehicle that is owned by a used vehicle dealer and is on the books of that used vehicle dealer and is NOT on record with any governmental secretary of state for licensed or titled since it is driven on dealer plates. He just received a CARFAX REPORT on this vehicle. This CARFAX report reflected 0 open recalls and 5 months until the next needed oil change. This can only happen if CARFAX had access to the dealer's I.T. system that services this vehicle. This individual has not approved their vehicle information to be shared by the servicing dealer to anyone. If this was a California dealer, it is possible the dealer is violating California law by unauthorized sharing of this customer's service history and very likely other "confidential" I.T. data.

Dealers need to stop this before they have to pay fines for releasing confidential information. Please read last month's issue of this newsletter.

Solution: Step 1 is to identify all third parties that have access to your I.T. data. You can easily obtain those that have direct access through your current I.T. vendor. Step 2 and subsequent steps will be covered in the future.

Public Auto Company 2019 Results

We consider the following 6 public company new vehicle dealerships. Some of their 2019 metrics were as follows:

	Asbury	Autonation	Group1	Lithia	Penske	Sonic	Overall (avg)
Annual Sales (billion-$)	6.9	21.4	11.6	11.9	22.8	10.0	14.1
Pre-tax Net Profit % Sales	3.3	2.5	1.8	2.9	2.7	0.8	2.3
Stock Market Value % Sales	40.0	17.0	11.0	14.0	15.0	9.0	19.0
Pre-tax Earnings % Stock Price	8.0	14.0	15.0	20.0	18.0	9.0	14.0
Stock Price/After Tax Net Earnings	8.0	8.0	7.0	7.0	7.0	11.0	7.0
"Blue Sky"/Pre-tax Profit Per Share	11.0	6.0	7.0	4.0	5.0	8.0	7.0
Working Capital % Annual Sales	1.6	3.6	3.6	0.1	4.2	0.2	0.5

As you know, the NADA reported pre-tax net profit % of annual sales has an average of approximately 2.4% the last few years while the above reflected 2.3% in 2019. Overall, they do not perform differently than privately-owned new vehicle dealers; interesting. We have reflected in the past what the factory required working capital for its new vehicle dealers is as a percentage of annual sales which approximates 3.5%. As you can see from the above, the actual working capital for two of the public companies exceeds this 3.5% and the other four public companies working capital are substantially less than 3.5%. It looks like the factories have two standards of working capital for their dealers (interesting and discrimination). The last metric above is a multiple of pre-tax earnings to determine Blue Sky value (intangible value). The range is 4 to 11, a very wide range. For most non-public new vehicle dealers this multiple on reasonable earnings might be 4 to 7.

Dealer Expectation Performance Survey

We had a four question survey sent to a large number of dealers in late May and received over 100 dealer responses. The answers were as follows:

53% expected June 2020 sales to increase from 2019 0 - 15%.
50% expect third quarter vehicle sales in 2020 compared to 2019 to increase 0 - 20%.
43% expected June 2020 service sales compared to 2019 to increase 0 - 15%.
41% expected their pre-pandemic employee levels to be 90 - 100%.

Bank Relationships

Most non-factory floor plan lenders usually have a large number of documents to sign as part of their floor plan lending and capital loans. Factory lenders would typically include Toyota Motor Credit, Ford Motor Credit, Chrysler Credit, etc. They are less burdensome with their paperwork and financial covenants. Some of these non-factory lenders have agreements that are unusually long with wordy terms and are not dealer friendly.

Loans are due if the dealer dies. These lenders say “trust” us. Never trust lenders with verbal deals. Do you want your family burdened upon death by your bank? Doubtful.

We know of one lender who has 4 pages to define the interest rate being charged.

Some of these lenders have metric ratios that some dealers are in violation of when they sign the “violated” agreement. When asked about it they say, “trust us.” Don’t.

With the vehicle business so good and interest rates so low, these lenders are “friendly” today. How do you think they will treat the marginally profitable and lower net worth dealer when business is not so good?