POWER STEERING

Steering your dealership to higher profits

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April 2016 profits for new vehicle dealerships trended the same compared to March 2016. This means 50% as many dealers made more pre-tax profits in April 2016 than compared to March 2016. Typically, April is a down profit month compared to March each year. Also, as you can see below, there are still 5-10% of dealers losing money.

April Profit Trends

	APRIL BETTER THAN MARCH	APRIL WORSE THAN MARCH	APRIL BEST MONTH	APRIL 3.0% PROFIT OF SALES	APRIL LOSS MONTH	APRIL LOSS Y-T-D
CHRYSLER	60%	40%	55%	35%	5%	0%
FORD	50%	50%	30%	30%	0%	5%
G.M.	45%	55%	25%	25%	15%	5%
IMPORTS	50%	50%	30%	25%	10%	15%
OVERALL	50%	50%	30%	25%	10%	10%

Nationwide, as reported by Automotive News, reflects April 2016 new car and light-duty truck sales were better than the most recent six years. May 2016 new car and light-duty truck sales were better than April 2016, but less than May 2014 and May 2015. This changes the trend where each month of the year was better than the same month of the year for prior years.

Federal Government Regulations

We were recently involved with a conventional real estate mortgage with a high income individual. They were obtaining a $300,000 first mortgage on a property worth more than $400,000. This would be considered a solid real estate loan. The first signing and initialing of the required loan documents included 29 signatures and initialing. At the closing of the loan at a later date, another 20+ signatures and initialing were required. In total, there were over 50 document signatures and initials. Our federal government is responsible for this burdensome process. Imagine the costs caused by the federal government to complete a conservative first mortgage on residential property.

"If you don't value your time, neither will others. Stop giving away your time and talents. Value what you know and start charging for it."
– Kim Garst

Inside

Low Used Front-End Gross Profit Margins

We receive and review a lot of factory financial statements each month. The first metric we look at after observing whether the dealership is profitable is the front-end used retail gross profit margin. Remember, the overall average is in the $1,700 - $1,800 range. When we see a low gross profit margin that is below $1,200, we often find out that the dealer is using a third party internet inventory-pricing service for their used vehicles. The dealer uses this service with the intent of better appraising the used vehicle to be bought or traded in or to price it to sell. The dealer using this service believes they are better off financially with lower grosses and believing they have a cleaner used vehicle inventory. We usually find these dealers are making a mistake using these internet services for various reasons. We find their front-end used retail gross profit margins averaging less than $1,200, down to $600-700. We also find their net profit as a percentage of sales or gross profit plus other income as a percentage of sales to be below average. We recently took the bottom 20% net profit percentage of sales of a group of new vehicle dealers which reflected a profit margin of 0.9% when the average dealer is over 2.0% of sales. The ratio of new retail units to used retail units was .9 – 1.0. The average used retail profit margin was $1,043 and several less than $800. Their ratio of used retail to new retail sales has not changed or has not changed materially since implementing this new inventory service. If you have low used retail gross profit margins and use an internet-based used vehicle service, we suggest you contact them to find out how you may be mis-applying their service so you can obtain average front-end gross profit margins or stop using the service.

New Vehicle Gross Profit Margins

Within this newsletter we typically indicate the front-end new vehicle gross profit margins reflected on a new vehicle dealers monthly financial statements. Though it is hard to believe, some dealers show extremely low new vehicle gross profit margins. This includes dealers making less than $400 per new unit sold, not even making holdback, and in some cases, actually reporting a loss on the sale of their new vehicles. We have seen this occur for GM dealers, and at times, Toyota, Honda, and Nissan dealers. How can this keep happening? Sometimes, it's due to factory stair step programs, factory incentive plans to dealers, or extreme pressure from the manufacturer to sell more vehicles. Who thinks reducing front-end gross profit margins will sell more of that dealer's model and not just take away sales from same make competing dealers? Dealers hope to make up for these low grosses at some point in the future. Sometimes they try to make up for these low grosses or loss grosses by earning more factory money that is put into other income and/or increasing the pressure to generate F & I department income. We don't believe the factory causing and creating these grosses is good for the dealer, the factory, or the customer in the long run. We also don't believe the advertising that goes with these grosses creates the image the factory wants from a CSI perspective. This just shows us that the factory talks about how important CSI is, but we don't think many of them care enough or are smart enough to realize what they are doing.

Interest Rates

As we all know, current interest rates are extremely low. Though the Federal Reserve raised the federal funds rate last year, 0.25% (target 0.25%-0.5%), the overall borrowing rates for floor plan, capital loans, and real estate loans (mortgages) remain historically low. The current official prime rate is 3.50% and the 3-month LIBOR rate is 0.65%. We hear from dealers and other business persons about paying off dealership real estate loans and home mortgages early. We almost always suggest this is not a good idea when the mortgage interest rate being paid is so low. Generally, we do not believe it is financially smart to pay off long-term low interest rate loans prematurely. We advise that if a dealer has excess cash funds, they should pay down new and used vehicle floor plans. Most feel interest rates will go up and the long-term interest rates on real estate will be less than the dealership's floor plan interest rate. It might make sense to refinance real estate loans to take advantage of current low rates. You can use this cash to pay down floor plan as long as the current real estate mortgage rate is only slightly more than the floor plan rate.

Factory New Vehicle Sales "Requirements"

We regularly find dealers receiving factory reports where the factory is reporting to the dealer that they are not new vehicle sales effective. Sometimes dealers ignore these notices. You should never ignore these notices and always respond while probably obtaining guidance from an automobile attorney. When we become aware of these notices, we ask the dealer to send the notice along with a map of the area showing the factory geography and census tracks assigned to the dealer. It is often obvious that the assigned market area has apparent errors in it to the detriment of the dealer. This includes other same make dealers closer to the certain area of your market both in air miles distance and/or drive time. At this time, dealers should seek professional help. Even if the factory ignores your letter or email or report you pay for, you do have it on record.

Balance New Vehicle Inventory

We had several GM dealers call and complain about not being able to obtain certain new vehicle inventory models. It is obvious that either GM still has not figured out how to allocate and balance new vehicle models or they are sending these “short” models elsewhere. For example, the below email was sent to us. We have edited it to protect the dealer from GM actions.

“Showed GM employee I had only 10 new cars on the lot. We had not been allocated a XXXXX from 2 ½ months, though we sold 2 per month last year. The only XXXXX in stock was purchased as a dealer trade. How many sales is GM losing when they cannot supply a balanced inventory to its dealers? It would seem someone in upper management at GM would resolve this problem they have allowed to develop and continue.”

Federal Government Medicare

All new vehicle dealers and their employees pay taxes into the federal government’s Medicare insurance program. This tax-benefit program started back in the 1960s. Many individuals believe that once they become eligible for Medicare insurance that their health care insurance premiums stop. We know one couple who are paying over $9,000 per year for their joint Medicare. What a shock this was to the couple that thought their health insurance premium costs stopped at age 65. We have a recent medical bill for services rendered to this couple. Below is a sample of charges to Medicare and the amount to be paid by Medicare:

AMOUNT OF BILL	AMOUNT PAID BY MEDICARE
$ 50.00	$ 8.52
$ 756.00	$ 143.58
$3,487.00	$ 818.91