POWER STEERING

Steering your dealership to higher profits

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September 2018 was a down profit month as would be expected based on monthly new vehicle sales history when compared to August 2018. As you can see below, 75% of dealers in our survey of over 200+ new vehicle dealers, in over 15 states, had reduced profits in September 2018 compared to August 2018. We normally expect profits to be less in September each year as is shown below. Hardly any dealers had their best month of the year in September, and only 15% of dealers made 3.0% or better pre-tax profits as a percentage to their total sales. The average dealer has been reflecting pre-tax net profit as a percentage of sales 2.3% for 2017 and 2.3% through July 2018. The number of dealers losing money has increased the last few months and is reflected below.

September Profit Trends

	SEPTEMBER BETTER THAN AUGUST	SEPTEMBER WORSE THAN AUGUST	SEPTEMBER BEST MONTH 2018	SEPTEMBER PROFIT 3.0% SALES MONTH	SEPTEMBER LOSS MONTH	SEPTEMBER LOSS Y-T-D
CHRYSLER	15%	85%	5%	15%	15%	10%
FORD	30%	70%	0%	20%	30%	10%
G.M.	30%	70%	0%	5%	30%	15%
IMPORTS	20%	80%	0%	20%	20%	15%
OVERALL	25%	75%	0%	15%	25%	15%

We have all read where new unit sales are "down" or going down and how "awful" that can be. We believe the authors of these "negative" comments do not realize that if nationwide new vehicle sales are around the lower 17 million unit range, 2015-2018 (2018 annualized), that there is no reason profits, which is what counts, would go down materially. Nationwide, pre-tax profit margins have been in the middle 2% range since 2010 and have been in the range of 2.3% - 2.8% for the years 2010-2018 (2018 annualized). We think most dealers would find it acceptable to have nationwide new vehicle sales remain in the current range of 17 million with the pre-tax profit margins remaining in that range.

"Success is not the key to happiness. Happiness is the key to success. If you love what you are doing, you will be successful."

-- Albert Schweitzer

Inside

Dealership Employees

It might be time to briefly review all of your employees in order to get a head start on 2019. Terminate any low performing or disruptive employees. It is not likely the low performing employees can be improved enough to keep. We do hear dealers say they will get rid of these low producing employees when they can find better replacements, but often nothing happens. If you do get rid of these low producing employees now it will "force" you to hire replacements sooner. We also find many dealers do not have enough sales people and recognize this but do not have enough effort to increase their needed sales person count.

In regards to "disruptive" employees, we hardly ever find they improve and often they get even worse. These "disruptive" employees discourage your other good employees and can cause "legal" problems for the dealership. Based on this reasoning, get rid of them now before they get even worse.

Review the annual compensation plans and see if any employees are grossly overpaid and if any employees are materially paid less than they should be. Now is a good time to redo pay plans for the new year.

Compare your employee staffing levels in each department to see where you might be too high and then try and adjust.

New Vehicle (Front-End) Profit Margins

As you can see in the enclosed profit survey, the new unit front-end gross profit margins are only $993. Also you can see many dealers with much lower new front-end gross profit margins and several dealers with negative (loss) new front-end gross profit margins. However, you can also see that even these low new front-end gross profit margins dealers are still achieving reasonable overall pre-tax net profit margins. There are a couple of reasons for this. One reason is other income, mostly generated from new unit sales, is so large at times that if this new other income were added back to the reported low new front-end gross profit margins, the overall new unit front-end gross profit margins will yield modest but reasonable results. Also, for most stores new units often generate less than 40% of the total of overall dealership gross profit and other income.

New Vehicle Sales Effectiveness

As we have written in the past, it is suggested that dealers regularly review how effective they are in selling new vehicles. Is the dealer selling enough new vehicles that they are 100% new vehicle sales effective? Often times the factory views this 100% metric as average. For example a dealer could be 90% and 9 out of 20 in new vehicle sales effectiveness. Normally being 9 out 20 is not a "bad job," but often the factory would call this a "bad job." There are also concerns about the accuracy of the factory's measurement of new unit sales effectiveness. There were two cases earlier this year where the factory lost termination cases because the dealers were less than 100%. For various reasons, the legal system found the factory's scoring system to be severely flawed. We also know of a market where there is only one major import franchise. In such a market some would expect the one major import and all domestics overall to be average, but based on this example, all the dealers in this market should be above average overall to be considered average (difficult concept at times to understand).

Used Vehicle Gross Profit Margins

As you can see the overall used front-end gross profit margins are approximately $1,705. If you remove the very low used gross profit margins from the sample, the overall used front-end gross profit margin will approximate $1,800 or slightly more. Many dealers reflecting less than $1,400 used front-end gross can improve these grosses. It is often due to lack of sales skills and sales intensity that yields below average used front-end gross profit.

Some third party vendors tell dealers with lower grosses to reduce their inventory in units, by getting rid of aged units, which will result in more used retail volume and increased F & I & SC income. We do not find dealers selling more units carrying a lesser day's supply. We also fault the logic of increasing F & I & SC income because this can be improved regardless of day's supply of used or front-end gross of used.

Wholesaling Vehicles

Dealers retail many of the used vehicles they take in on trade and buy from other dealers and auctions. Many dealers seem to wholesale too large a percentage on the used vehicles not retailed.

In many cases this is a mistake. Since it is so “hard” to obtain used vehicles for retail, some dealers should re-assess the used vehicles wholesaled. Some dealers take the easy way out for disposing of used vehicles in the wholesale market. We would suggest all dealers look at the used vehicles they have been wholesaling and see if some can be kept for retail at reasonable gross profit margins and possibly increased used retail sales.

New Vehicle (Net) Floor Plan Interest Expense

The enclosed survey reflects NEW FLOOR PLAN INTEREST EXPENSES LESS FACTORY INTEREST CREDITS. This overall amount reflects the metric averages only $5 per new unit sold, a very small net expense. By factory: Chrysler $40; Ford $154; GM minus $124; Import $48; and overall only $5. These amounts will vary by how much the interest credits are by factory along with the day’s supply of new vehicle inventory. You can see some dealers have a negative net new vehicle floor plan interest expense. This can happen if the factory pays, for example, a 90 day’s supply credit of interest and the dealer carries less than a 90 day’s supply of new.

Year-End Planning

We have included our annual year-end accounting and tax planning document. Please share it with your office manager, CFO, and/or bookkeeper. Call or email us with any questions or comments.

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