

Steering your dealership to higher profits

A publication of Michael Silver & Company and
Woodward & Associates
Consultants to the Automotive Industry

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May 2009

Monthly Profit Trends

March was an improved profit month for new vehicle dealers. Only 15% of our 200 new vehicle dealers showed a loss in March, and those that had losses were smaller. As you can see below, approximately 5% of new vehicle dealers lost over \$20,000 in March. In past years, March was one of the best profit months of the year. This trend seemed to hold for March 2009. Fortunately, the number of new vehicle dealers that are in a loss position for the year, though high, continues to improve.

	Mar. Better Than Feb.	Mar. Worse Than Feb.	Mar. Loss Over \$20,000	Mar. Loss Month	Mar. YTD 2009
Chrysler	50%	50%	5%	20%	50%
Ford	70%	30%	10%	25%	25%
General Motors	70%	30%	5%	15%	20%
Imports	80%	20%	10%	15%	35%
Overall	70%	30%	5%	15%	30%

As reported in *Automotive News*, dealers sold 820,000 new cars and light duty trucks in April 2009 versus 1,249,000 units in April 2008. If you annualize April 2009 year-to-date new car and light duty truck sales, 2009 will show 9,072,000 units for the year, the lowest expected annual new car and light duty truck sales in over 30 years. The franchises that show the smallest sales reductions include Hyundai, Kia, Subaru, Volkswagen, and Audi. All of these franchises have decreases less than 20% compared to the same time period in 2008.

Financial Institutions

All dealers have retail installment contracts that are funded by financial institutions. Dealers usually send the financial institution a copy of the factory invoice or some description of the vehicle including options. If the dealer makes a mistake by listing options not included in the vehicle and if the financial institution discovers the absence of these options, the dealer can be required either to submit reimbursement for the missing options or to purchase back the current balance of the contract if the vehicle is repossessed.

Recently, one of our dealers was called by a financial institution that had purchased a retail installment contract. This institution told the dealer that the vehicle was represented as having a sunroof and a theft deterrent system, though it did not have either. As a result, the

financial institution wanted a large payment from the dealer. The dealer found that both items were in fact on the vehicle and said that when they called this financial institution, the personnel there explained that they were receiving a lot of calls of this nature. The dealer felt it might have been an attempt by the financial institution to fish for dealers who would pay without questioning the charge. Let your finance department and office know about this story in case they are called on such a matter.

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New Vehicle Dealership Buy-Sells

The sale of new vehicle dealerships has slowed down to a trickle in the last nine months. Since last summer, new unit sales have been down drastically and profits have been down to their lowest level as reported by the National Automobile Dealers Association. Dealers show a 1% net profit as a percentage of sales and a return on equity being 12.4% for 2008. The last time the return on sales was this low was in 1991, when it was also 1% and the return on equity was only 14%. The long run return on sales, though it has been declining over time, is 1.6% with a return on equity of 24.7%. Also, *Automotive News* reported that total new car and light duty truck sales in 2008 were only 13,200,000 units, the lowest since 1992. If you annualize March 2009 year-to-date new car and light duty truck sales (which were only 2,200,000 units as reported by *Automotive News*), 2009 new car and light duty truck sales would be only 8,800,000 units, the lowest since 1978.

In light of these financial and new unit sales results, the number of buyers for new vehicle dealerships are nearly nonexistent. However, there are some buyers out there who feel they can make a reasonable profit, even in these times. Listed below are some of the areas of concern the willing buyer needs to consider before purchase.

1. Make sure you prepare a detailed financial model or projection of expected sales based on the reality of today and realistic obtainable profits at today's sales levels. You need to be able to project making at minimum a 25% return on your investment with conservative projections; otherwise, pass on the deal.
2. Consider making sure you can get out of the real estate if the dealership does not perform. Consider this question: If you purchase the real estate, will there always be a new vehicle dealership wanting to use the real estate being purchased or a factory wanting a dealership at this location? If not, then pay for what the real estate is worth if it is not used as a dealership. If you lease the property, you need to be able to get out of the lease if the franchise fails, is materially changed, or if the dealership is unprofitable.
You need to have a reasonable rent factor whether you purchase or lease the real estate. Rent factor would be defined as rent, amortization and depreciation of the facility, mortgage interest, property taxes, and building insurance. The rent factor should be around 1.1% of sales or 7% of total dealership gross profit for a dealership's building that is not a new facility.
3. Make sure you have financing in place for the dealership purchase before you sign the purchase agreement. You need to have a lender that you can count on to stay with you for your working capital loans, floor plan loans, and real estate loans. We do not like to see and do not see in all cases loan covenants with lenders. It is our opinion that if the lender does not want to do business with us, all they have to do is give us reasonable notice, and we will go to another lender. In today's times, you cannot count on the lender staying with you or the ease in finding another lender. You need to have a loan agreement with your lender stating that the lender cannot abandon you if you are meeting some reasonable financial guidelines.

In summary, go slow when purchasing a new vehicle dealership in these financial times. If it does not look like a real good deal, then pass on the purchase.

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**Even when people are more successful than they had imagined,
nothing is ever achieved without giving something up.**

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GM and Chrysler Dealers

With Chrysler filing for bankruptcy and the possibility of GM filing for bankruptcy, dealers need to consider whether they always want to sell a new vehicle when they have the opportunity. If you have a chance to sell a new vehicle with a \$1,000 gross and the factory rebate assigned to you by the retail customer is \$4,000, it is possible that you might not collect all or anything on this vehicle sale. In bankruptcy, the court will decide. Therefore, you might want to pass on selling this vehicle since there is the real possibility you might not collect the \$4,000 rebate, and thus lose \$3,000. Several alternatives exist in this scenario, including not selling the vehicle, having the customer take the low interest rate program, or having the customer take the risk of collecting on the \$4,000 rebate.

Dealership Performance

Many Chrysler and GM dealers are finding out that their franchise contracts might not be renewed, with one of the reasons being that their scores by their factories show them as non-performing or below average as a dealer. GM has a scoring system called DART, which is made up of four categories:

	Weighting
New vehicle sales effectiveness	50
CSI	30
Capital (working capital)	10
Profitability	10
Total	100

We have seen dealers with DART scores as low as 75 to over 130. Unfortunately, some dealers are unaware of their scores or of their factories' scoring system. If you are unaware of it, we suggest you obtain the worksheet showing your factory score. In areas that you are below average in, consider how you may improve these areas, as it might cost your franchise in the future if you ignore them.

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The worst sorrows in life are not in its losses and misfortune, but its fears.

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