POWER STEERING

Steering your dealership to higher profits

A publication of Woodward & Associates
Consultants to the Automotive Industry

Written by Carl Woodward **October 2019**

August 2019 was an improved profit month as compared to July 2019. As you can see below, these metrics are from over 200 new vehicle dealerships, 25% of dealers had their best month of the year while 30% of dealers made 3.0% + pre-tax profit net of sales. Profits overall remain good for dealers since 2009. This is the longest period of time for new vehicle dealers with good profit trends in at least 40 years.

Monthly Profit Trends

	AUGUST BETTER THAN JULY	AUGUST WORSE THAN JULY	AUGUST BEST MONTH	AUGUST 3.0% + PROFIT OF SALES	AUGUST LOSS MONTH	AUGUST Y-T-D LOSS
CHRYSLER	65%	35%	35%	20%	5%	10%
FORD	50%	50%	20%	30%	20%	20%
G.M.	70%	30%	30%	20%	20%	15%
IMPORTS	50%	50%	25%	40%	10%	15%
OVERALL	55%	45%	25%	30%	15%	15%

Nationwide *Automotive News* reported year-to-date new unit sales including fleet sales through September 2019 was 12,730,000 and for 2018, 12,942,000. The year 2019 is 98% of 2018. As a reminder, Ford, Chrysler, and General Motors decided for "flawed" reasons not to share their monthly results. Based on market share: Ford is down; Toyota is down; Chevrolet is down; Nissan is down; Jeep is down; and Dodge is down for the higher volume franchises. However, dealers overall profit margins remain good. This new vehicle volume for the industry works for most dealers.

Illinois Property Taxes

Some states have higher sales taxes, income taxes, and property taxes. At times these states have an outflow of population which is not surprising. We have a recent "valid" appraisal for one of our Chicago area new vehicle dealerships. We also looked up their annual real estate property tax bill. This dealership had an appraised value of $4.8 million and an annual property tax bill of $350,000. This works out to an effective tax rate of 7.3%. In downstate Illinois, we often find the effective tax rate percentage to be approximately 2.5% of the fair market value. What is the tax percentage rate for your dealership?

"Success is liking yourself, liking what you do, and liking how you do it."
– Maya Angelou

Inside

Government Mandated Overtime Changes

As you may remember, the federal government attempted to change the rules for paying overtime, time and one-half compensation premium, several years ago, but it failed in the legal system. Now the federal government has again changed the rules for which employees could possibly be paid overtime now, where they were not paid the overtime premium in the past. This new rule goes into effect 1/1/2020. The annual compensation amount for certain employees where they will have to be paid overtime is $35,600.

We have a suggestion on how to deal with this financially for those employees that will now qualify for this "overtime" premium pay and a pay raise. Our goal with this article is to not have a material compensation expense increase for the dealership. Step 1 is to determine those employees that are included in the new rules. Step 2 is to determine the current annual average weekly compensation for each employee of this group of covered employees. Step 3 is to determine now, on average, how many hours per week are overtime hours, those hours exceeding 40 hours. Step 4 is to re-compute a lower hourly rate for this group of employees so that after this lower hourly rate is determined, the revised compensation, including the overtime premium compensation, will yield the same annual compensation to the employee. It is suggested you try and explain to your employee that they are now being paid hourly and will be making approximately the same total compensation as before. It's just being computed this way due to federal government law. The following example illustrates how the changes would apply to a salaried employee consistently working 50 hours per week and earning $600 per week. This employee would qualify for an additional $60 per week in pay under these new rules, as compared to earning the same wages on an hourly basis.

The hourly rate is computed by using the average hours per week over 40; in our example it's 10. Multiply it by 1.5 which is 15 in our example. Determine the percentage of 40 hours to the total of 40 hours plus the premium hours at 1.50; 55 in our example. The percentage is 72.73%. Multiply the percentage times the current weekly pay which comes out to $436.38 in our example, then divide by 40. The new hourly rate is $10.91.

The below example shows you the key differences. The employee will now be paid overtime and make the same total compensation as before while the dealership has the same compensation expense and follows the new overtime compensation rules. If you have any concerns regarding our suggested procedure and to make sure it is legal and accurate, you should consult with your attorney.

	Weekly-Current	Weekly-New
Regular earnings for pay period	$600.00	$436.38
Regular hours per week	50	50
Hourly rate	$12.00	$10.91
Overtime premium	-0-	$163.62
Total Compensation	$600.00	$600.00

National Financial Metrics

The National Automobile Dealer's Association (NADA) published monthly certain year-to-date metrics in a report called Average Dealership Profile. Certain of the August year-to-date metrics include:

Average monthly sales	$5.2 million	increase slightly from 2018
Net Profit Before Tax	$991,000	increase slightly from 2018
Net Profit % of total Sales	2.4%	increase slightly from 2018
New units sold retail	581	down slightly from 2018
Used units sold retail	511	increase slightly from 2018

Used Vehicle Value Changes

We have read more than one article about how used inventory values are down so much. Many readers will read such articles and find them credible and believable. We were not sure. We had someone take 20 of the most popular used models, 2017 (3 year old model - today) from the current Black Book using "clean" and the same 20 models, 2016 (3 year old model from last year's Black Book). Though there were a few models that varied, overall there was no material difference in total value. The current value for these 20 used vehicles was $374,000 and from a year ago, $373,000. What this indicates is there was no material change of used 3 years old models from October 2019 to October 2018.

Blue Sky - Goodwill - Franchise Value

We are regularly involved in assisting in the sale and purchase of new vehicle dealerships. We have seen deals in the last year, more than one, with Blue Sky exceeding $50 million. We have also seen some very small amounts of Blue Sky for very small dealerships. There are still many in the industry that lean to believing that Blue Sky might be some multiple of “earnings.” There are several definitions of “earnings,” not being discussed in this article.

What should the Blue Sky be for a dealership that has been losing money? Many believe the answer might be zero. This is usually not the case. For those dealerships, except very small dealerships, that make a small amount of profit, or are losing money, these stores are almost always worth some Blue Sky. Though some dealers would pay no Blue Sky for this dealership, many knowledgeable dealers will pay Blue Sky based on “expected” profits. As we tell dealers all the time, subject to the rent factor not being too high, almost all dealers are worth some Blue Sky. Even if you are a buyer and think this low profit dealership is worth little or no Blue Sky, there are always dealers that will pay Blue Sky on expected profits, though discounted by some amount.

Used Retail Vehicle Sales

Most of our dealers with some exceptions sell more used retail vehicles than new vehicles. This ratio is less for many import dealer franchises. We have had a handful of new vehicle dealers make a “real” effort to materially increase their used unit retail sales where they had been selling many more new retail units compared to used retail units. We read an article in *Automotive News* about a Texas dealership group increasing its used retail unit sales to new retail unit sales from a ratio of .5 to 1 to over 1.5 to 1. What does this mean? If the right kind of effort is made, dealers can move the “peg” on the sale of used units.

Employer Health Plans

Dealerships pay a certain varying amount for their employee health insurance premiums. Depending on the location of the dealership, whether unions are involved, and the competitive situation, the gross premiums a dealership pays varies greatly along with how much of the gross premium is paid by the dealership. This includes family plans and those that just cover the employee and no family members.

As was written recently in the *Wall Street Journal* (9/26/2019) the annual premium exceeds $20,576. On an hourly basis, based on 2080 hour year, this amounts to approximately $9.89 per hour.

Parts Department Metrics

As you can see in the enclosed survey, we have reflected the parts department overall gross profit margin. The overall average is 33%. This is approximately the same over the four dealership groups.

You can see the lowest margin being 26% while the highest margin being 46%, with the median at 33%.