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New Vehicle Sales Can Still Generate Long Term Profits

Most dealers are struggling with declining gross margins on new cars sales. This trend has been occurring steadily over the last ten years. The problem is even more pronounced given the recent declines from a sluggish economy. Many dealers are trying to focus their attention away from new car sales and concentrate where the profits are occurring by looking at gross profit percentages by department. A look at these average gross margins may seem to support this:

- New Vehicles - less than 6%
- Used Vehicles - 10 to 15%
- Parts - 30 to 35%
- Service – 60 to 70%

Although gross profits on new cars are the lowest in your store, they still drive the profitability of other departments. The following is how new vehicle sales will impact your other department:

Used Vehicle Department

1. New car sales generate desirable trade-in vehicles, which can be sold at a higher gross profit.
2. Some trade-in vehicles will enter your certified pre-owned programs. The certified programs are very desirable for certain customers and will generate more floor traffic.
3. As a new vehicle franchised dealer, customers for used cars perceive you as more reputable than an independent dealer. This will generate additional floor traffic.

Parts and Service Department

1. Consumers that purchase new vehicles are more likely that service their vehicles at your store than owners of used vehicles. New vehicles sales are the engine that drives the parts and service department. Although used vehicle sales generate higher grosses in many cases, customers that purchase used vehicles are more likely to service their vehicles at independent garages.
2. Most warranty and recall work will be created from your new car sales.
3. Trade in vehicles received from a new car sale will be reconditioned in your parts and service department.
4. Trade in vehicles received from a new car sale may enter your certified used program, providing additional work for the parts and service department.

Finance and Insurance

1. New vehicle sales will likely account for over half of the gross profit from your F&I department.

Let's look at an example. You sell a new vehicle for \$30,000 to a customer that lives in your community with a limited gross profit. At the same time the customer buys the vehicle, they also trade in a \$15,000 vehicle. Your service department reconditions the unit for \$1,000 and you sell the trade in with a gross profit of \$1,500. You also sell the customer a \$500 extended warranty contract and maybe a finance contract. Finally, the customer has all their service and warranty work performed at your store for the next four years. Even though you make a limited profit on the new vehicle, you are creating reasonable gross profits in your, parts, service, used car, and F&I department. Without thinking long-term, many dealers would turn down this deal and lose the residual benefits.

Dealers need to look at the profits of the dealership as a whole as opposed to just individual departments. The long term profitability of the used, parts, service and F&I departments is contingent on the number of new cars you sell today. Strive to increase new vehicle sales even if your "grosses" decline as you will make it up in your other departments.

Downey & Company, LLP specializes in management, finance and taxation of automobile dealerships. For more information, please call Paul McGovern at 781.849.3100 or send an email to pmcgovern@downeycocpa.com.

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