

Batten Down Those Hatches

By Phil Villegas

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If you own a dealership selling one of the Detroit 3 brands, you might be thinking the franchise is worthless.

If you believe everything you hear, all you should expect to receive from the sale of your dealership is the value of the real estate and cost of your assets. The value of the “goodwill” or “blue sky” for domestic dealers seemingly is nil.

The theory is that every Honda, Nissan and Toyota dealer is making money while every Chevrolet, Dodge and Ford dealer is losing money. Nothing could be further from the truth.

Having the “right” franchise does not guarantee success any more than having the “wrong” franchise dooms you to failure. Individual dealership success has as much to do with the management and culture of the store, as it has to do with the brand.

While it may not be hip, sexy or green to ally yourself with domestic dealers in the current environment, there is a fundamental flaw in concluding domestic franchises are worthless.

Stereotyping doesn't work when judging people and it doesn't work when judging dealerships. Every dealership needs to be evaluated on its own merit and performance in conjunction with the franchise brand.

I wish several of the very profitable domestic dealers I know would sell me their dealerships for the cost of real estate and assets. This would be like winning the lottery!

A dealership's goodwill or blue sky is the intangible value of the business, and like any business, the greater the potential of the business unit, the higher the blue-sky value.

The evaluation of intangible value is based on several

factors in addition to the current market performance of a brand. The following eight factors should be considered:

- Market performance of the brand.
- Past performance.
- Future potential.
- Geographic location.
- Competitors in the local market.
- Customer base.
- Quality and track record of management.
- Specific cost structure of the business (including facilities).

In assessing the above factors in today's environment, the true challenge facing the domestic dealer body has less to do with the value of its brand, and more to do with the number of domestic retail outlets.

Fundamentally, there are too many in comparison to import dealers. The resulting cannibalistic environment deteriorates a dealer's ability to compete on product against import dealers. There were on average three domestic dealers for every import dealer at the beginning of the year. Therefore, on average, import dealers sold three times the monthly volume by franchise that domestic dealers did.

As a result, it is easy to mistakenly evaluate the collective values of domestic brand dealerships as being inferior to imports. The fact is, retail business units that have and can sustain high levels of profitability will command the highest intangible values, irrespective of brand.

It is hard for any retail business to have a competitive market value when on average it sells 30% of the retail volume of a competitor, particularly when many of the semi-fixed and fixed costs are the same. Adding to the challenge that many domestic dealers face is that their facilities are not “right-sized” to their retail environment.

Unfortunately many domestic dealers have facilities that exceed the current product demand, adding operating cost pressures many import dealers do not encounter.

But, if you are a domestic dealer with monthly new retail sales in excess of 75 units per month and your rent factor is less \$300 per retail unit (new and used), your dealership is a viable business unit and should command some intangible value.

(Rent-factor example: Domestic dealer sells 75 new retail units and 35 used retail units, 110 total retail units × \$300 = \$33,000.)

The toll of the over-weight domestic dealer body is resonating more during these times of economic slowdown. This is one of the most challenging times auto manufacturers and retailers have faced with little, if any, signs the storm will let up in the near future.

Economic uncertainty caused by the housing market and exacerbated by high fuel prices is the key catalyst to our current market conditions. People are just hesitant to make any major purchases, including vehicles (regardless of the brand).

The shift to fuel-efficient small vehicles in the last few months will begin to level off and stabilize. Fuel at \$4 a gallon was the tipping point for a segment of the population, the point where fuel efficiencies outweigh cost, comfort, styling and safety, and the point where losing \$10,000 on a trade made more sense than spending an extra 50 cents a gallon of gasoline.

While the cost of fuel affects many Americans' purchasing decisions, it does not overshadow the comfort and safety of the family. As uncertainty regarding the economy wanes, so may apprehension of purchasing a new vehicle.

As with everything in life, level heads will prevail, and the same will hold true for the domestic dealers. We must recognize the current market conditions for what they are and realize it will be a little while before things get better.

While the current transformation we are witnessing unfortunately will cause the demise of many domestic dealers (and some imports, too), the downturn ultimately will be healthier for the industry as a whole. I dread the pain and heartache any dealer has to face in this market

environment. But I also recognize that those dealers who can weather the next nine to 15 months will come out much better on the other end, particularly the domestic dealers.

There is no doubt import dealerships command a higher intangible value, but to completely write off domestic dealership values as a whole is shortsighted and can prove to be a costly missed opportunity in the long run.

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