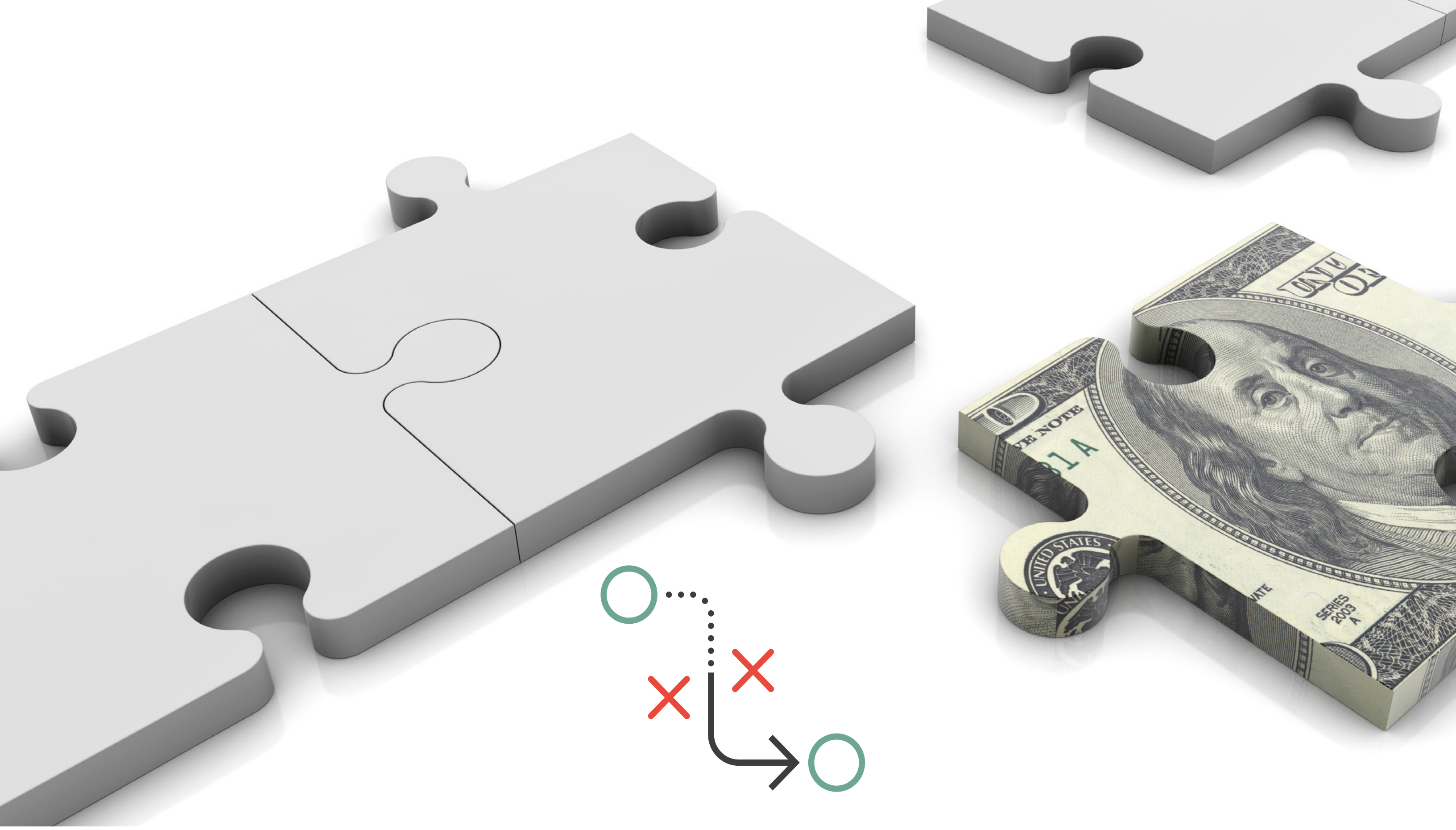

Dust Off Your 2008 Playbook

You Might Want to Forget the Great Recession, But Its Lessons Are Worth Remembering in the COVID Era

BY ERIC FIFIELD

If you put 2008 in an archive box marked "Do Not Open," you might want to rethink that designation.

As independent dealers begin planning for 2021, there are some valuable lessons to be remembered from the difficult year of 2008 that can prove beneficial.

Don't see the correlation between a financial crisis-based recession and a pandemic-fueled slowdown?

Let's take a brief look at some historical data points.

LOOKING BACK TO LOOK FORWARD

The origins of the 2008 and 2020 crises are very different.

In 2008, unsustainable levels of debt existed, as well as a lack of credit quality. The combination of ever-increasing levels of business and household debt created a bubble that was ripe to pop, prompting the economy to come to a screeching halt.

Debt-laden companies and financial institutions quickly declared bankruptcy, followed by spiraling home foreclosures and unemployment.

The current 2020 economic slowdown is rooted in a challenging health crisis that is quickly becoming cyclical in nature, with initial damage being felt in both the supply and demand portions of the economy.

One positive to note is that businesses and consumers have less debt than in 2008. Additionally, the financial system as a whole appears to have more capital and is healthier overall.

Clearly, regulatory and behavioral changes implemented after the Great Recession have prepared business and consumers to better weather the current crisis.

All that said, there are some similarities in the situations.

Both 2008 and 2020 dealt a severe blow to employment.

In 2008, corporate staffs were the first to feel the effect, followed by middle- and low-income jobs.

The reverse is true for 2020. Nationwide shutdowns and social distancing have impacted low- and middle-income jobs first, and we are now finally seeing corporations cutting higher-wage positions.

Stimulus packages are another similarity, though the recipients are different.

In 2008 there were enormous corporate bailouts, while 2020 stimulus was focused on consumers and smaller businesses in the form of loans and relief checks.

That flow of cash buoyed the economy during the summer months before the spigot was turned off in the third and fourth quarters of last year.

Some economists believe that economic impact of the COVID-19 pandemic could be far worse than the 2008 recession, resembling more closely the Great Depression of the 1930s.

So what does all this mean for you?

THE DOW JONES PARALLEL

In a perfect storm of economic events such as in 2008 and 2009, the used car market can behave like the Dow Jones Industrial Average.

In fact, there are several parallels between the stock market and the used car market when supply exceeds demand. Both operate on the simple economic principle that prices rise when there are more buyers than sellers and fall when the reverse occurs.

In 2008, used car values plummeted at first as demand dried up while the supply kept on going. The excessive used vehicle supply was eventually absorbed, but at much lower prices.

In the years that followed, however, used car values rose dramatically as cash-strapped consumers re-entered the car market in force.

We're already seeing a similar trend with used car prices that could extend well into 2021.

Beginning in March 2020, as the shutdown was in full swing, nearly every passenger vehicle on the road lost value.

Used car values plummeted because of an excessive supply of cars at auction. The problem was exacerbated by hesitant bidders, who were concerned about selling existing inventory or fearful of further pricing pressure.

Cash-strapped rental car companies and commercial fleets quickly reduced their fleets due to lower demand. Dealers lost their floorplan credit lines, which forced lenders to move their collateralized vehicles to auction.

Off-lease volume was estimated at a record-high 4 million units this year, which meant lenders had significant off-lease inventory to unload in the wholesale market.

But by the third quarter of 2020, used vehicle inventory tightened dramatically as stimulus-supported consumers sought out the best deals they could get.

The lack of new inventory production from manufacturers and dramatic declines in public transportation created a perfect opportunity for independent dealers to significantly increase unit sales.

For 2021, many variables remain in play, including the potential success of virus containment measures, speed of financial response and the state of the economy.

All of those variables are enough to make anyone's head spin.

As an independent auto dealer, you cannot press pause – you don't have that luxury.

So let's focus on three lessons learned from the Great Recession that can be applied going forward to increase your chances of success.

LESSON 1: RELATIONSHIPS MATTER

Many of the tools for doing business have changed dramatically since 2008.

Fax and couriers have been replaced by ubiquitous connectivity and secure portals for completing business transactions. Money is transferred nearly instantaneously versus the three-day hold on a cashier's check. And the required handshake now is more likely to be a distant hand wave during a video conference call.

But some things do not change.

A strong lender relationship continues to be a requirement for running a successful independent dealership.

But there are some new aspects to that relationship.

In the past, only small or less-capitalized institutions were interested in working with independent dealers. Often viewed as poor profit targets, independent dealers often struggled to find the right lenders willing to work with their customers.

The automotive retail market has changed dramatically since then, thanks to the growth of used car chains.

The lending institutions willing to finance those used cars have changed as well.

Credit unions used to dominate the space, given their less stringent underwriting requirements. Now lenders of all types are looking at the independent automotive space as a potential revenue stream.

But not every lender is a good fit for an independent dealer – and that's where the relationship comes into play.

It's critical that the dealer principal and the auto lender have a clear understanding of each other's business processes and financing requirements.

That's not just an annual casual conversation over lunch. It's a symbiotic relationship built over mutual understanding and business respect.

That also means tightening your team's compliance practices and training your team on how to select the right lending institution based on the credit application.

Remember, lenders pay close attention to the number of contracts you send that they cannot fund. The more non-fundable contracts sent their way, the more likely they will be to take their business elsewhere.

The same can be said for their close ratios. Called look-to-book, lenders carefully examine how many credit applications they approve with your dealership compared to how many they close.

If they approve several applications and only close one, you have a problem.

What this all boils down to is you don't want to send a credit application to every lender you work with. Rather, select the lender(s) that are most likely to approve and close on the loan.

Working with lenders requires attention to detail and finesse, regardless of whether it's 2008 or 2021.

LESSON 2: WHAT MAKES YOUR DEALERSHIP DIFFERENT/BETTER/BEST?

In 2008 and '09, strategic independent dealers were dipping their toes into the certified pre-owned market as a differentiator.

The benefits of a CPO program were significant.

CPO helped ease consumer concern over purchasing a used unit by ensuring the vehicle's quality. It also helped visibly demonstrate the benefits of purchasing with a given dealer.

Additionally, independent dealers were better able to increase the base cost of the units because of the perceived quality of their inventory. And CPO programs created a great bridge to the F&I discussion to increase vehicle service contract penetration.

If CPO was not a viable option, independent dealers looked into complimentary limited powertrain protection, which gave a similar benefit of increasing the perceived value of their inventory and creating greater opportunity for F&I product upsells.

But many independent dealers had two potentially glaring issues standing in the way of their using those programs to their fullest potential – they did not have a service department and/or they did not have the inventory to qualify for a CPO program.

Since 2008, independent dealers have become even better problem solvers than in previous years. In 2021, it's even more important to think outside the box when it comes to overcoming challenges that can force you to leave money on the table.

Start with inventory. If you know you want to incorporate a CPO program or a complimentary powertrain

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protection program into your operation, you need the inventory to support it. And that means competing with franchise dealers for late-model, low-mileage vehicles.

But rather than competing with franchise dealers head-to-head at auction, consider developing a relationship with a local car rental or leasing company so you can sell their off-lease inventory.

Also remember the benefits of securing trade-ins when consumers are looking to trade up. You can almost always purchase a trade-in vehicle for less than you would pay at auction.

Let's say your inventory is taken care of. The next step is actually inspecting and making any necessary repairs to the vehicles for certification.

Don't have a service bay? No problem. There are plenty of mechanics near you who need the work. Develop a relationship with them to handle all your CPO needs.

LESSON 3: IF YOU BUILD IT, THEY WILL COME

CPO and lifetime powertrain warranties should be used as strong market differentiators for independent dealers targeting value-conscious consumers who still want to purchase a nice vehicle with years worth of value remaining.

The millennial and Generation Z demographics are the perfect targets.

During the Great Recession, the millennial generation suffered tremendous economic and employment hits. They entered the workforce during the heart of the recession, meaning they had to compete for entry-level jobs with people who were much more qualified and out of work.

That labor pool glut forced millennials to either go back to school or enter the underemployed workforce.

Either way, that highly educated group became saddled with staggering student debt that still has the potential to topple the economy.

A 2018 report by the Federal Reserve Bank of St. Louis found while millennials make up 38 percent of the workforce, they are at the greatest risk of becoming a "lost generation" for wealth accumulation.

Now the same can be said for Gen Z (born after 1996). That demographic is beginning to shoulder some of the largest student loan debt the country has ever seen.

With lowered economic opportunities and staggering student debt, those consumers are searching for greater value for their dollar.

Independent dealers can carve out a large slice of the target available market by proactively promoting the benefits of CPO and lifetime powertrain warranty offerings to those demographics.

Those benefits include:

- A more reliable vehicle and higher purchase satisfaction.
- Risk reduction of costly repair bills and the typical concerns of purchasing a used vehicle.
- Additional coverage options available to buy with confidence.

During the Great Recession, a fair amount of mystery surrounded the potential revenue of an F&I product within the independent space. Sales and F&I teams received little training, lenders were few and far between, and customers were just beginning to see the value of the products.

Fast forward to 2020, and the majority of independent dealer principals count on F&I revenue to meet their financial goals,

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lenders realize "protected" deals carry less risk and consumers see warranties as a guard against unexpected expenses.

Now there are many F&I products designed to meet the needs of every customer.

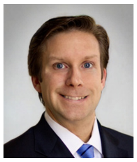
Still, some of the mystery remains.

These days, dealers should closely evaluate their inventory and their customer demographics to create specific market-differentiating packages to meet everyone's needs.

After all, what works for a millennial with a family of four might not work for a single Gen Zer working two jobs.

While 2008 might seem like eons ago, the valuable lessons learned then still apply in 2021.

While we can only hope the return to health and prosperity does not take as long as the recovery from the recession, we must prepare to make the best of whatever comes our way. ■



ERIC FIFIELD BRINGS MORE THAN 28 YEARS OF AUTOMOTIVE INDUSTRY EXPERIENCE TO EFG COMPANIES. AS CHIEF REVENUE OFFICER, HE IS RESPONSIBLE FOR CLIENT DEVELOPMENT AND ACQUISITION, AS WELL AS HOLDING THE TEAM ACCOUNTABLE FOR SETTING CONTINUOUSLY HIGHER STANDARDS AND PROVIDING CLIENTS WITH THE HIGHEST LEVEL OF EXPERTISE AND ENGAGEMENT.