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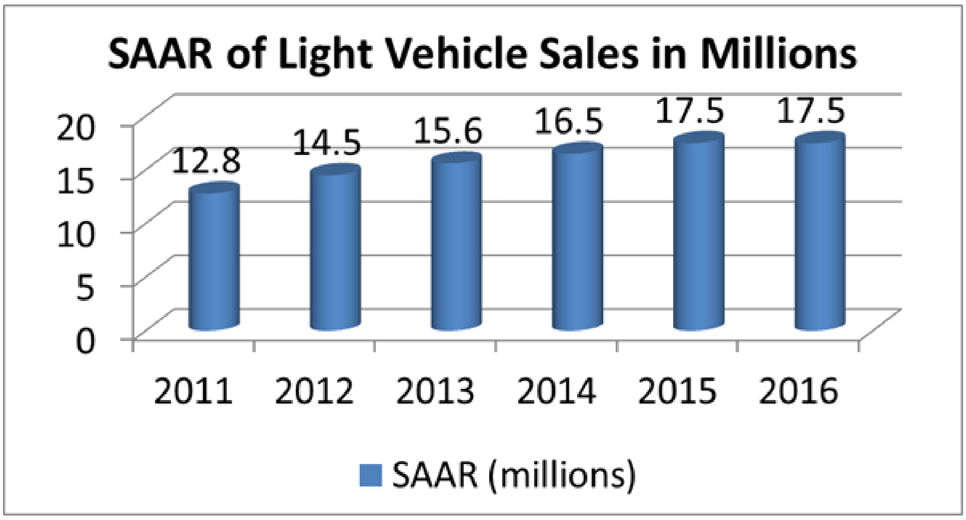
The State of the Automobile Industry

AUTOMOBILE, BUSINESS ADVISORS, BUSINESS VALUATION
BY SCHNEIDER DOWNS PROFESSIONAL

The automobile industry experienced a great year in 2015 with annual sales of light vehicles (SAAR) reaching an all-time high of 17.5 million units. As shown in the chart below, the automobile industry experienced significant growth from 2011 to 2015, as the economy recovered from the early recession in 2008 through 2010.



This growth was the result of a combination of various factors such as low interest rates, low unemployment and pent-up consumer demand due to the earlier recession and consumers delaying car buying. However, in 2016 growth started to taper off. Haig Partners reports that, although sales were still high, 17.5 million units, without the increase in fleet sales, SAAR would have declined, since actual retail sales on new vehicles declined from 2015 to 2016. Since fleet sales are less profitable, margins for 2016 began to decline. Profitability also declined as the result of increased general and administrative costs such as higher wages and facility expenses. The NADA profile for average dealerships reports that earnings before tax averaged 2.7% in 2015 and declined to 2.5% in 2016.

Now what is expected for 2017? In an article published on April 5, 2017, the NADA reports that new car sales are expected to hit 17.1 million units in 2017. A major factor in car buying and the performance of the auto industry is interest rates. When interest rates are low, customers are incentivized to buy a new car. Also, low rates have a significant impact on the bottom line of a car dealership, since an automobile dealership finances car inventory with debt (also known as floor plan debt). Although interest rates are still low, the Federal Reserve Open Market Committee (FOMC) increased the federal funds rate by 25 basis points in December 2016. The FOMC is expected to increase the rate further in 2017. Despite this fact, the Chief Economist for the NADA, Steven Szakaly, reported that the NADA is hopeful that any decline in sales due to higher interest rates will be negated by rising consumer incentives. However, profits might still take a hit due to higher interest rates.

The value of a dealership is largely dependent on the Blue Sky value (goodwill), which is determined by multiplying a market multiple times pre-tax earnings. Haig Partners reports that with the exception of luxury brands, most Blue Sky multiples are still at peak levels. However, if profits decline, the value of an automobile dealership will likely decline as well.

Christy Samek specializes in valuing automobile dealerships for estate and gift tax planning purposes. Valuing a business requires significant judgement in determining the correct approach and assumptions. If you need help in determining the value of your dealership, please contact Christy Samek at 412-697-5415.

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SOURCES: SAAR DATA FROM GROUP 1 AUTOMOTIVE 10-K'S FOR 2010 THROUGH 2014 AND 2015 AND 2016 SAAR DATA AND OTHER DATA AS CITED ABOVE FROM THE HAIG REPORT – YEAR END 2016. ALSO, INFORMATION AS CITED ABOVE FROM THE NADA AT WWW.NADA.ORG.

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