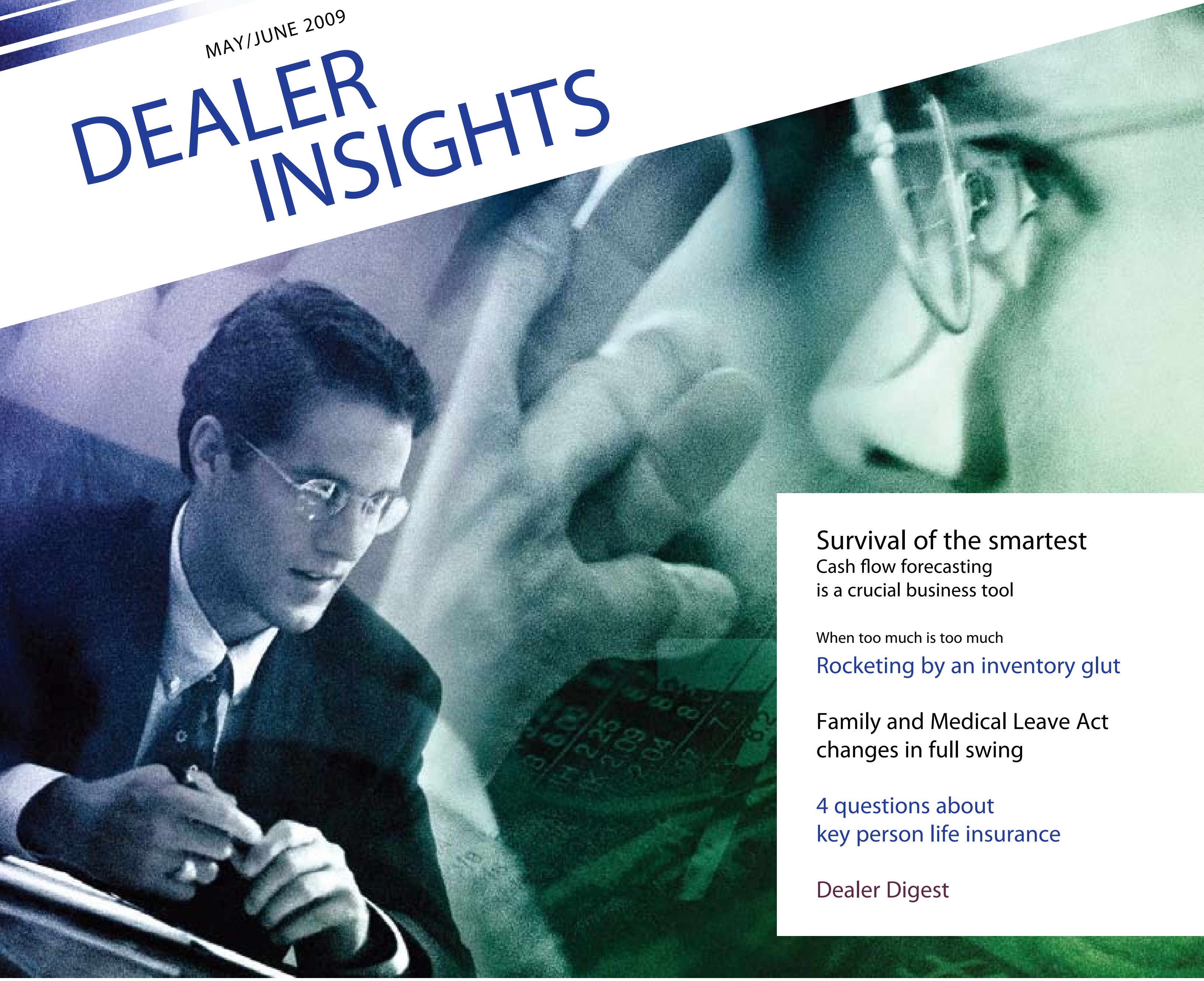
MAY/JUNE 2009

DEALER INSIGHTS



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Survival of the smartest

Cash flow forecasting is a crucial business tool

Cash — it pays your operating expenses, which, in turn, allows you to open your doors each day. It lets you keep good relationships with creditors and helps you feel optimistic about your dealership's performance. Cash, simply put, makes the (business) world go round.

But, in these times of rapid economic contraction, dealers biting the bullet can struggle with the flow of cash as sales shrink, expenses persist and trade payable terms seem to get shorter. All of these are reasons why dealers should forecast cash flow in an economic downturn.

What is cash flow forecasting?

Cash flow forecasting is a systematic process to predict the sources and amounts of cash that will roll in over a certain period — and the recipients and amounts of cash that will flow out during that same interval.

Cash flow is *not* profitability. Profitable dealers have destroyed their credit or gone out of business waiting for enough money to come in to meet payroll and other obligations. If you're honest with yourself, don't overestimate the current market and rely on concrete information, a cash flow forecast is a valuable business tool.

Where do you start?

Forecast for the time increment that's best for your dealership, whether it's a year, quarter or month. Begin with real data and collect actual bills and records for that time period. Use information about the basics: fixed and variable expenses, estimated sales and cost of sales, all based on your general ledger and other records. Then follow these three steps:

1. Review your expenses for the last quarter or for whatever amount of time you've chosen to forecast. Fixed expenses include overhead, wages and other stable costs. Use those numbers to project your fixed expenses for that period. Don't get bogged down in history, but use this data to make your predictions informed.

Be sure to include variable costs such as advertising and sales commissions. You may be unable to forecast precisely how these expenses will change, but you can chart them for a year to identify trends and establish averages. To ease forecasting, group costs and expenses into departments, such as new cars, used cars, service, parts, finance and insurance.

2. Approach your income forecast in the same way. Avoid guesswork and base your forecast on what you know you can reasonably count on. For example, use new and used vehicle sales figures from corresponding previous periods adjusted to your current sales patterns.

You can group like income, such as new car sales, used car sales or service department revenue. But remember that much of your income is likely to lag behind the actual sales or service department work. So enter those figures accordingly to reflect current patterns.

3. After estimating your expenses and income for your target time period, enter them in monthly categories. Use categories such as utilities, payroll, inventory, and sales and taxes to get a snapshot

Priorities, priorities, priorities

Forecasting cash needs accurately isn't enough for dealers in distress, who need to prioritize their cash disbursements for maximum effect. Fortunately, cash disbursements can be determined — and prioritized — more easily than a revenue forecast.

Floorplans typically are paid first, followed by certain fixed overhead costs such as rent, utilities, salaries, payroll taxes, and monthly loan and lease payments. Other operating expenses are next in line. What remains is usually allocated to trade payments.

All disbursements need to be prioritized and forecasted. For instance, your dealership might establish that it has a payroll every two weeks and will pay its nonfloor vendor invoices in 45 days. This cash disbursement activity, to make sure it's completed, should be constantly updated in spreadsheet software or another easily readable format.

of what you'll need and what you'll receive each month. Seasonal fluctuations will be evident, as will any noteworthy trends (dwindling SUV sales, for example), and you can plan adjustments in advance.

After your forecast is in place, use it to measure your actual performance and see where adjustments are needed.

Is it worth it?

Cash flow forecasting is a valuable tool that helps to keep your books in order, your bills paid and your operation positioned for future growth. It certainly takes some work, but you'll likely find it well worth the effort. ■

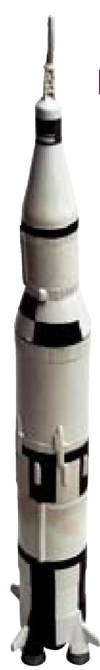
When too much is too much

Rocketing by an inventory glut

"Houston, we've had a problem." Although that famous line from the Apollo 13 moon flight is about a malfunctioning spacecraft, it also applies to overstocked auto dealerships.

If your dealership has too much money tied up in inventory, it could hurt your cash flow — or even cripple your mission entirely. So like the astronauts on that hugely challenged Apollo 13 mission and their overseers in Houston, you'd better think of some creative ways to get yourself out of this jam pronto.

The new above-the-line sales or excise tax deduction for new auto purchases is expected to help boost sales, and if it does, a decrease in inventory will follow. Here are some other measures to consider.



Management as mission control

Obviously, to prevent overstocks from hurting your dealership, you need to avoid them in the first place. And you can do just that by regularly evaluating your inventory control tools and establishing some best practices for sustaining a feasible volume.

To get started, take another look at any "rules of thumb" you may follow. For example, one line of thinking holds that your inventory-to-sales ratio should be about two to one. If you plan to sell 50 units, you should keep at least 100 vehicles on your grounds.

But does that work for you today? Now more than ever, you may want to team up with other dealers selling the same brand to reduce your new-car stock. Just make sure these "pooling partners" are close enough geographically to make sharing practical, but far enough away to avoid direct competition.

In addition, order only what you know will sell quickly. Closely track pattern failures in any or all of the vehicles you stock. Meet with your financial and technology advisors regularly to discuss whether you're getting the inventory data you need, and to look at what new vehicle-tracking hardware and software has hit the market.

Also, if a used car customer is interested in a particular vehicle that's not in stock, keep a record of the request. Put this document in a shared (electronic) place that all sales people can reference in the event that the vehicle comes into inventory later.

Fueling up on Internet strategies

Slow days at the dealership have an upside. Use the extra time to evaluate your Web site and online practices with the simple goal of moving more stock. Remember, most buyers do homework on the Internet first, and you want potential customers to linger on your site — not skip off to your competition's.

For starters, if you haven't already, try using video on your Web site. In e-business, videos are believed to be effective in getting customers to act. What's more, there are as many as 12.7 billion hits to watch videos on the Internet each month, according to eMarketer, a Web research firm. It estimates that, by 2012, 88% of all Internet users will be video watchers. So the audience is there, but so is increasing pressure to produce videos that are interesting. One Midwest auto dealership, for example, features quarterback Brett Favre in its video. But if you can't afford a sports star, vehicle walk-arounds can be the first step toward getting a customer into your store. Video testimonials from happy customers also can be a powerful tool. So if you have a collection of complimentary letters, follow up with these customers about doing a video shoot.

You also could create a short video explaining how the sales or excise tax deduction for new cars works. (And if you don't put this info into a video, make sure you include it in other advertising materials.)

Tools for making a good, effective video are available. For instance, in January the dot-com company YouTube was offering free tools to let any dealership edit and post a promotional video and analyze its viewership.

While you're considering your video options, also review how you handle e-mail inquiries you receive via your Web site. One good approach is to number incoming e-mails and respond to them accordingly.

If you go this route, make sure everyone understands the process upfront and then hold staff accountable for getting back to prospects as quickly as possible. Periodically review the system by examining how your staff followed up on e-mail leads over, say, a 24-hour period.

Rising above competitors

Always do your homework to make sure your prices are competitive, and that these are the prices you're advertising. A few specific strategies to look into include:

Pricing vehicles for subprime (and other) buyers. Some dealers look for vehicles they can buy $1,000 to $1,500 under wholesale book, believing that allows them to cover their lenders' fee structure and still make a good gross profit. One industry consultant, however, holds that:

- ❏ Better profit opportunities exist with current-year models, not yet in a retail book, where lenders advance a percent of like-invoice,
- ❏ Program, rental fleet sales and auction vehicles may offer good profit opportunities compared with selling only retail trade-ins,
- ❏ Some new vehicles with factory rebates structure well, as do some lower-priced new vehicles with available cash-back rebates allowed by some lenders, and

- ❏ Manufacturers' online auctions are a great place to learn about lease returns, early terminations and repossessions, and you can shop the "virtual inventory" with your customer at your side.

As far as used cars are concerned, at press time their values were dropping and considered likely to continue to drop. So pay special attention to used car pricing and reconsider how much working capital you want tied up in them.

Making used cars seem new. Reconditioning is an investment. For example, put new tires on a used vehicle to boost both curb appeal and customer confidence. Replace aging or torn stickers — they make a car look like it's been sitting around too long.

Also, save leftover new car brochures for the used car department. Putting them to use gives the used car buyer a new car feeling. And rotate the lot display weekly to perk up customer interest; put newer arrivals in your best display locations.

Catering to women. It doesn't matter if they're going to buy the vehicle, drive it or only give their opinion: The word is that women dominate car-buying decisions.

But ask a female customer and she's likely to say she doesn't want to be treated like a "woman." In other words, make sure your sales staff doesn't talk down to female shoppers. And remember, women typically don't want to negotiate with dealers — they want to trust you.

Not *quite* rocket science

Inventory management may not be rocket science, but it is a critical component of your dealership's financial success. For this reason, it's imperative that you stay on top of what's in stock and use creative thinking to get rid of what you don't need. ■

Family and Medical Leave Act changes in full swing

Is your dealership complying with the recent federal Family and Medical Leave Act (FMLA) changes that took effect Jan. 16? It's important to consult with your attorney to see, because failure to abide by FMLA rules could expose your dealership to considerable legal risk.

For instance, the new Military Caregiver Leave program lets employees take up to 26 weeks of leave in a 12-month period to care for a family member with a serious illness or injury incurred in the line of duty while on active duty.

Another new initiative, the Qualifying Exigency Leave program, gives employees with a family member in the National Guard or Reserves the opportunity to take up to 12 weeks of leave to handle certain issues connected to that person's active duty, such as attending a child's or spouse's welcome-home ceremony.

Other areas affected by the FMLA changes include:

Intermittent leave. You must now provide members of a military family as much time off as you give employees in other programs. For example, if you allow all workers a 15-minute coffee break, employees eligible under the new FMLA rules may take family medical leave in 15-minute increments.

Also, you can now require employees claiming to need intermittent leave for a chronic condition to have a medical provider recertify that need *every 180 days*, rather than every year as originally required.

Light duty. If an injured or disabled employee spends time performing "light duty," you can no longer count it as family medical leave. This effectively bumps up the total time that the employee may be away from work. "Light duty" isn't defined, but it's generally understood to mean less demanding work requirements that conform to the employee's limitations.

Concurrent leave. You can require that employees take any time available in paid-time-off programs — such as vacation or sick time — *at the same time as* family medical leave. This helps limit the total time an employee may be away from work.

Bonuses and awards. You can now deny a bonus or award to employees who take family medical leave as long as you treat employees who are away from work for another reason in the same way.

4 questions about key person life insurance

Imagine that the most important person at your auto dealership — in terms of your bottom line — died or was disabled. What effect would the death or absence have on your dealership's financial health for the next month? The next six months? The next year?

Key person life and disability insurance can avert financial problems when an owner or pivotal employee suddenly stops contributing to business operations. Here are four questions to ask when considering this coverage:

1. Why buy it? As beneficiary, your dealership can use the proceeds of key person insurance to compensate for a temporary drop in productivity — and the ensuing financial loss — while a key person is out of commission.

The proceeds can provide cash to supplement the business while you locate and train a replacement as well as fund a shareholder or partner buyout in accordance with a buy-sell agreement. (Note that a key person policy is separate from traditional disability insurance, which provides a disabled person with income.)

In addition, many banks require that dealerships buy life insurance for owners and other key people as a form of collateral. Key person coverage ensures business continuity and the repayment of outstanding debts.

2. How does it work? With the key person's consent, the dealership typically pays the insurance premiums and is the policy's owner and beneficiary.

Premiums are not tax-deductible, but death and disability benefits generally are exempt from income tax. Some dealerships assign the benefits of unused life and disability insurance policies to key employees upon retirement as a perk.

3. Whom should it cover? The owner-dealer is the most obvious key person. Others might be your top salesperson, marketing director or service manager.

4. How much does it cost? Although cash is currently in high demand for many dealers, an investment in key person insurance can be invaluable if tragedy strikes. Insurance rates are based on several factors, including the insured's age, physical condition and health history.

The *type* of insurance policy — for example, term (less expensive) or permanent life insurance — also affects cost. Ten- to 20-year terms with level premiums are popular options. Although more expensive, permanent life policies build up cash value that can give the dealership a line of credit in times of need.

The amount of desired coverage also affects your premiums. For each key person, estimate how the loss would affect sales, service and morale. Some individuals are more valuable to your business than others. Various metrics — such as replacement cost and business value — may be quantified to make sure your dealership has adequate coverage. ■

DEALER DIGEST

Leasing IT: Dos and don'ts

If you're hurting for capital, consider leasing IT equipment as one way to free up dollars. Ideally, you'll get a continuing stream of state-of-the-art equipment, you won't need to worry about disposing of the old stuff, and you'll be able to take a liability off your balance sheet.

Unfortunately, IT leasing is rarely that simple. If you're going to fully reap these benefits from a leasing arrangement, follow these dos and don'ts:

Do look at the big picture. Assess your IT needs over a three- or four-year timeframe, and evaluate leasing for your entire business rather than on a department-by-department basis.

Don't violate contract terms. Let's say business is slow and you don't need as much equipment as you thought you did. If you return some of it, you're likely to find yourself still responsible for the remaining payments.

Do be especially alert to end-of-the-lease terms. Watch out for burdensome premiums for buying out equipment.

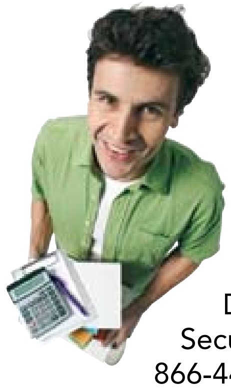
Don't slip up. If you return equipment late or misplace it, you might be forced to keep making monthly payments or buy out the contract at a premium of the original equipment cost.

Do use IT asset-management practices. Specialized software can help you keep track of exactly what equipment is where, when the lease expires and so on.

In the aggregate, IT and office machines are among the largest categories of leased equipment, second only to transportation equipment, according to the Equipment Leasing and Finance Association. ■

IRS/DOL offers small employers free guide on 401(k) enrollment

A new publication to help small employers understand automatic enrollment for 401(k) plans is now



available. *Automatic Enrollment 401(k) Plans for Small Businesses* gives an overview of the benefits of starting and operating this type of 401(k) arrangement.

Free copies of the booklet are available by calling the Labor Department's Employee Benefits Security Administration toll-free at 866-444-EBSA (3272) or by visiting the agency's Web site, dol.gov/ebsa. ■

5 tips for buying a VoIP system

When it comes to capital investments for the rest of the year, remember that vendors are dealing with the same revenue challenges as everyone else — and may be offering some bargains to keep their cash flowing. For example, if you're interested in buying a Voice over Internet Protocol (VoIP) system, consider these five shopping tips:

1. Get competitive bids by putting out multiple requests for proposals (RFPs).
2. Make sure vendors respond with performance specifications and define all terms not in general use; be wary of ambiguous statements and generalizations.
3. Sign a multiyear contract for software or maintenance if you're expecting to grow after the downturn ends.
4. Consider a hosted or managed version of the technology.
5. Be ready to change providers down the road — especially for support services.

Also, try to get extra features and functions bundled in your purchase. Some of the top VoIP innovations of 2008 included service for the iPhone and the Android, the extension of voice-streaming technology to video, and voice-to-text transcription for both incoming and outgoing messages. ■