Does the Internet Mean the End of Solid Gross Profits?

From an interview with Pat Ryan, Jr., CEO and Co-Founder of INCISENT Technologies.

If anyone's trying to convince you that you can't earn a profit because of the Internet, they don't understand the Internet.

High and Low Margin Products Inherent in Retail

Has the Internet put an end to strong gross profits?

This is a question every retailer faces, but in other industries retailers understand their higher and lower margin products. Interestingly, dealers traditionally haven't thought about having high and low margin products in their pre-owned cars, instead focusing on earning the same target profit on every deal. In order to suceed with your customer, you need to understand which are your high and low margin products and manage your business accordingly.

What Makes a High Margin Product?

Since everyone competes to acquire inventory in the same wholesale market, a high margin product is typically a popular, high demand vehicle with more limited supply setting up stronger gross profits. Essentially, consumers want it and the demand is greater than the supply. Let's use Cash for Clunkers as an example. Dealers had a slow 2009, but at the end of Cash for Clunkers there was still a high demand for new cars. Toyota dealers had only 15 days of supply of many new cars and those cars were selling at or around sticker price (a price they were not obtaining all year long). As soon as the demand increased and the supply decreased, vehicles turned quickly at strong pricing and profits.

CARMAX: Famous Fast Turning Retailer

CARMAX is a famous example of a fast turning retailer. If you look back at their history, they turn inventory quickly yet their average gross profit is actually higher historically than NADA Dealers' average gross profit. How do they do it?

First, they understand which vehicles are high and low margin. When they have a popular car with short supply, especially with low mileage per year, they earn high gross profits. If it's a former rental car with a lot of supply and not as much demand, CARMAX recognizes it and prices accordingly so it will turn quickly yet with a lower margin.

To view a short video of Pat Ryan discussing how to maximize your margin with a strong turn, visit www.ConsumerOptimization.com

Pat Ryan, Jr. is the Chief Executive Officer and Co-Founder of *INCISENT Technologies*, maker of FirstLook Inventory Management Systems and MAX Internet Advertising and Marketing Systems. The Company was ranked as the #4 Fastest Growing Software Company in the United States in *Inc Magazine's* Top 500 List as well as the #1 Fastest Growing Company in the Automotive Sector.

Pat is widely followed as a thought leader and speaker and can be reached at pat@incisent.com.

Many Vehicles Turn Quickly and Earn Strong Gross

There are people in the industry that say in an Internet world, quick turns preclude you from earning solid profits. The best way to resolve this dispute is to look at the facts. A recent national sample of sales and profit, showed dozens of fast turning vehicles with strong (front end) gross profits such as:

- 2007 Corvettes $3,000+ average
- $2,000+ average
    - o 2005 RAM 1500's
    - o 2008 Lucerne's
    - o 2008 Yukon and Tahoe's

There are dozens more examples (of course the list is full of highline) but most interestingly, strong gross profit cars typically turn faster than low gross profit cars. Why? Because profit and turn are both reflective of demand.

Low Profit Cars Frequently Turn More Slowly

Interestingly, low profit cars often have slow turns. From the same recent National sample, slow turning vehicles with weak front end gross profits included:

- 2007 Audi A4 Sedans—$584
- 2007 Explorers—$861
- 2005 Nissan Muranos—$928

Why are they turning more slowly? Two reasons. First their inherent demand is lower. Second, dealers do not typically recognize those demand levels when pricing the vehicle and therefore do not price it for low margin and quick turn, until the vehicle has already begun to age.

Bottom Line: Succesful retailers need to understand which vehicles have the demand to justify pricing for profit and still turn quickly. Those vehicles that have lower demand should be priced for lower margin to turn quickly from the beginning.

How Can Dealers Know Which Vehicles Have High and Low Demand?

- For vehicles with strong history at your dealership look at your average profitability, selling price, and days to sale for each vehicle to see your past demand.
- In addition, and for vehicles with limited or no sales history in your store:
    - o Look at JD Power PIN average profitability and days to sale for dealers in your market for indications of a specific vehicle's potential margin.
    - o Market Days Supply: Look at Market Days Supply for that model vs. other vehicles in your market to understand current supply and demand.