"An Ass For Every Seat"

Ted H. Schaar ©2018

A few years back I visited a car dealership to help our daughter buy a used Kia Rio. She identified the car she wanted online—and I researched pricing for it—so we arrived prepared. She wound up purchasing the Rio but getting there was unpleasant and time-wasting.

Before the deal was done, at one point, I said to her, "OK, let's go to another dealership," and we nearly got to the door before the sales manager intercepted us and said he could meet the price I thought the car should be at *after all*. Earlier, the same guy, probably around 40, said, "Do you think we should sell the car at a loss?" I replied: "What potato truck do you think I rolled off?" (Updating an old line because today few know what turnips are, including me at the time.) He didn't protest or offer any response because even he knew how lame his statement was.

When all of the foolishness was over, and we were exiting with keys to the vehicle, I looked at the waiting area and saw a variety of customers, individuals, couples, and small families waiting to be helped. It was a busy Toyota dealership. Without exception, every adult looked unhappy, apprehensive, even miserable. Women clutched their purses, men looked wary.

What is it about purchasing a car that makes it notably disagreeable to most Americans? Buying a computer or refrigerator doesn't stir the same anxiety; neither does buying a house, so it isn't just a matter of the dollars involved.

Edmonds.com, which bills itself as, "...a car-shopping website driven to make car buying easy..." surveyed "1,002 adult (18+) car owners/intended owners" in 2014 and titled its press release on the study: "When it comes to car shopping, Edmunds.com finds that Americans hate the haggle so much, they'd give up sex, Facebook, and smartphones to avoid it."[1] That's extreme!

An article in the *New York Times* reports on car-buying services such as Authority Auto for people who don't "want the anxiety of haggling for a car."[2] Testimonials on the firm's website attest to its effectiveness. One includes, "I put buying a car right up there with dentists visits, getting mugged, or almost earning a Darwin Award! I wish this business [Authority Auto] had been around much longer for my other car-buying painful experiences, but they are now and I am a happier human for it, too."[3]

Various aspects of the transaction make the experience unique: cars are expensive, every accessory adds to the cost, options are "packaged" driving up the price, and everyone knows vehicles require ongoing expenditures—often high ones—to maintain and repair. Once out the door with your name on the title, problems with the car are *your* problems. During normal use—unlike most possessions—cars are subjected to violent forces ranging from the raging series of explosions that propel them (electrics are becoming more common but combustion engines still dominate) to the vagaries of roads and weather.

And most consumers understand vehicle pricing isn't rigid like it is for most products; it varies considerably.

Dealers portray markup as tiny; salespeople regularly say while holding up a thumb and forefinger separated by a quarter-inch, "there's not much room to negotiate." But easy-to-find information about selling prices as compiled by Edmonds, Kelley Blue Book, and other firms makes this suspect.

When I bought my first car in the 1970s I was able to dicker hundreds off the sticker price of around $5,000; it was a Chevrolet Monza which began rusting before the 36-month-payment book was exhausted. Disgusted, I sold it and bought a used 1973 Ford Maverick with low miles from a private owner. Rationale was I saw a lot of Mavericks and Mercury Comets, its sister car, on the road and figured they must be well made.

The only luxury the car had was an automatic transmission; otherwise, it was Spartan, no radio, not even a glove box. Its manual steering was so difficult I had to buy a spinner knob, often called a "suicide knob," mainly to help with parallel parking downtown. A straight six powered it, and there was enough space around the engine to peer over the fenders and see pavement nearly all the way around. I had some minor rust repaired and touchup paint applied, and it turned out to be a good buy. The Maverick had funky appeal as a medium-sized clunker with bench seats, got decent gas mileage, and took me everywhere in style and comfort for six years; then I sold it to nephew Bruce who drove the car to Texas where it ran well until it was totaled while parked on the street.

My next car was a Renault Alliance purchased new in 1985. By then my wife and I were subscribers to *Consumer Reports*, so I followed its advice on how to get a reasonable "deal." This involved test driving various possibilities to settle on a particular car and then ordering a computer printout—novel at the time—that listed the Manufacturer's Suggested Retail Price and dealer factory invoice "cost" for base vehicles and options.

Spreads between what the dealer supposedly paid and MSRP prices weren't much. The magazine advised offering $100 more than factory invoice. That seemed like an absurdly small amount of profit for the dealer, but the magazine stated there were other cash incentives such as "holdbacks"—additional amounts dealers receive *from* manufacturers once a car is sold[4] that might be as much as 3% of the MSRP. On a $20,000 car, that's $600, not a princely sum.

My freelance writing business was doing well, and I drove a fair amount for work-related reasons. Typically, I wrote in the morning and reserved afternoons for meetings with clients in Wisconsin and Illinois. Beginning in 1988, I started leasing cars and deducting allowed expenses on my tax returns. Wound up leasing five total, three Acura Integras, a Toyota Corolla, and a Honda Accord. By the time I had the last, communications technologies and the Internet made visiting clients in person largely unnecessary, primarily due to teleconferencing and e-mail, so I started buying cars again. First, a used 1999 Mazda Protégé, then a new 2005 Hyundai Accent.

Consumer Reports' recommendations for reliable used cars rated the Protégé high so I test drove one with low miles at a dealership, went back to my office, cut the deal on the telephone with the salesman, and faxed an offer-to-purchase at an agreed-upon price. When I visited the dealership to sign papers and pick up the car, cashier's check in hand, the sales manager told me the salesman was wrong on the price, and I needed to pay $50.00 more. Naturally I thought about going to the mat on principle but quickly decided making a big deal out of 50 bucks would be put me on the same level as that goof, so I wrote a personal check for the surprise extra, got the keys, and was on my way.

The Hyundai was more of a gamble but my brother had an Elantra, the next car up in the Hyundai line, and was happy with it. For the Accent, I purchased the *Consumer Reports* printout on dealer and MSRP prices as I had 20 years previously, test-drove the car, and then did most of the deal on the telephone.

Once we settled on a price, the salesman faxed an offer-to-purchase form. I filled it out, faxed it back, supplied a credit card number for earnest money, and all that was left to do when I visited the dealership was sign some papers, pay for the car, and endure a lengthy pitch for stuff I didn't want from the finance manager—I didn’t need a loan so this meeting was asinine from the start. Customers just want to get on with it, but the pitches seem endless and most are for practically worthless stuff, from special undercoating to added warranty protection. I was embarrassed for him which is just how I felt about the FM involved with my daughter's Rio purchase. Imagine doing that all day.

In terms of the "deal" I received, unlike most people, with cost data from *Consumer Reports* in hand, I had a clue but really was only guessing in terms of how the price I negotiated compared to what others paid for a car identical in every way except the vehicle identification number.

Sliding prices make me and others distrustful—I didn't want to be the one taken to the cleaners. Most feel the same way, hence the anxiety. However, a friend pointed out recently that "everyone thinks he or she got a good deal." Indeed. It's part of the crazy car-buying experience.

Even dealers evidently face flexible pricing. A friend related a story that while working for one as a consultant, his high-level-dealer-management contact received a have-to-take call with my friend present. Someone at a major automobile manufacturer was on the other end and the dealer manager chewed him out for giving better pricing to a competitor who carried the same line of cars.

In 2010, I gave the first Accent to our daughter and purchased a used 2008 Accent from a private owner; it now has 80,000 miles on the odometer and probably will go many, many more. From the rather basic automobiles I've owned, it's clear I'm not a car nut. I like cars but am too practical to go into debt for them. Decades ago I realized they are expenses.

By the time I helped our daughter buy the Kia, ten years had passed since I visited an actual dealer. It didn't take long to be reminded how irritating it can be. Cars are cool, so it's kind of sad it's the way it is. Customers don't trust dealers and certainly dealers don't and can't trust customers; consumers wear car salesperson hats when they are looking to trade previous automobiles. Many people are as comfortable lying as they are telling the truth and anyway, they probably reason, lying to car dealers is justified.

Dealers, manufacturers, etc. associated with automobiles (and most other enterprises) are in business for one reason: money. This often shadows more noble thoughts such as helping people get what they need first and want, second, at a fair price.

Many years ago the phrase "getting paid is fun" occurred to me. Money is crucial, it's *freedom*—at least in some ways. Accumulating it by taking advantage of the unwary is unacceptable to me and most others, but there are some who don't care how it's generated. For them it's a caveat-emptor-anything-goes world.

Although I often regret impulses, I had one that directed me to explore markup in the automobile business, and it led to this story. Invariably when the subject comes up people tend to opine that it is low, *very* low.

In the early 1970s, I worked for a music store in downtown Madison, Wisconsin. Each tag listed an item's retail price and, in a simple code, its wholesale cost. The store owner told me how to establish a retail price: "Double the cost so the markup is 50%," he said. He figured markup as a percentage of the *retail* price, so if the tag read $100, the cost was $50 and markup, 50% of the *selling* price. Telling this to Forry, one of my sharp brothers, he quickly said the markup was actually 100%. True. And it's common in retail although it is often expressed *after the fact* not before which makes the markup seem smaller.

For example, this is from entrepreneur.com: "Even though there is no hard and fast rule for pricing merchandise, most retailers use a 50-percent markup, known in the trade as keystone. What this means, in plain language, is doubling your cost to establish the retail price. Because markup is figured as a percentage of the sales price, doubling the cost means a 50 percent markup. For example, if your cost on an item is $1, your selling price will be $2. Fifty percent of $2 is $1, which is your markup."[5]

Not so fast. Another article from entrepreneur.com states: "Used by manufacturers, wholesalers, and retailers, a markup is calculated by adding a set amount to the cost of a product, which results in the price charged to the customer. For example, if the cost of the product is $100 and your selling price is $140, the markup would be $40. To find the percentage of markup on cost, divide the dollar amount of markup by the dollar amount of product cost."[6]

Brother Forry would side with the second article—$1 on $1—is 100%. Fifty percent of the retail price but 100% of the wholesale price. If most retail markup is 100%, why isn't markup in the automobile business 100%?

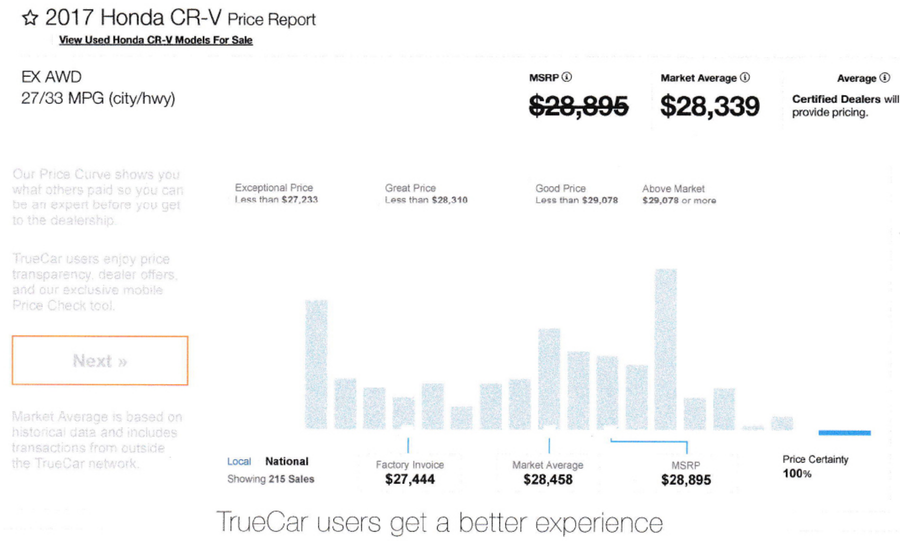
There is no doubt dealers make a lot of money. Edmonds reports, on average, each sells 945 cars annually,[7] and, according to Kelley Blue Book, new cars in 2015 cost $33,666 on average.[8] Multiplying by 945 indicates a typical dealer might have revenues from new car sales alone of more than $31 million annually.

For a current example of automobile pricing, I visited consumereports.org but discovered it no longer offers reports on car models that list factory invoice and MSRP. Instead I was directed to truecar.com (more about this later) and downloaded a report (below) on a 2017 Honda CR-V. My goal was to establish a baseline to work from.

The MSRP is listed at $28,895 but according to TrueCar, the market average, *what the car is really selling for*, is $28,339. The line through $28,895 in the graphic, according to TrueCar Senior Consumer Support Specialist Raymond G., "represents you should not pay that amount for the vehicle"; the small "i" inside a circle stands for "information." When clicked online it produces explanatory paragraphs.

For example, clicking "Factory Invoice" at the website brings up: "Factory Invoice is the amount that a manufacturer initially charges the dealer for a vehicle, including destination fees, regional ad fees, and other fees initially charged to the dealer by the manufacturer. This price does not include discounts, dealer incentives, or holdbacks (money allocated back to the dealer from the manufacturer upon sale)." In this explanation there is a lot of room for the dealer to pay less and earn more: "discounts," "dealer incentives," "holdbacks."

Without these sources of additional profit it's hard to imagine how dealers could survive. Looking at the graphic below, it appears they pay the manufacturer $27,444 for this vehicle but some evidently sell it for *less* than that. As surprising, most consumers evidently pay *more* than the MSRP.



TrueCar Report 2017 Honda CR-V.[9]

Over the years, when I've had questions related to vehicles, I've been successful *without exception* getting answers from members of the Antique Automobile Club of America.[10] I decided to ask a question about markup in the group's General Discussion Forum online:

"Hello from America's Dairyland. I'm exploring writing a story about how the automobile business operates. No, I don't believe dealers pay anything near what is listed on the 'factory invoice'; second, I've never seen a convincing story with information from insiders on how the business truly works; third, I'm not looking to make things harder for anyone. Goal is truth. I've had some experience in retail, and the typical markup is 100%—buy for $10, sell for $20. Sometimes, rather confusingly, this is referred to as a 50% markup, meaning 50% of the selling price is markup. My goal is to find individuals with long industry experience, interview them, and write a report. Please send an e-mail to deneb77@icloud.com if you're interested in helping and wish to remain anonymous or have opinions or ideas and wish to remain anonymous."

Various members replied, many citing industry experience. They mentioned markups on new cars ranging from 8 to 33%. However, it's not clear in every case how the percentage was figured. Some appear to be discounts *off MSRP*; others, percentages *above* factory invoice. In the following, I applied stated percentages off or above to the 2017 CR-V figures I received from TrueCar. This is for comparison purposes only, and the implications might not apply to every kind of vehicle, from largest to smallest, expensive to inexpensive, least popular to most popular or other ranges that might be named. Many factors affect pricing, some involving labor—from design to engine installation—and materials, others are indicative of fickle consumers who decide certain cars aren't desirable, which leads to discounting, sometimes *deep* discounting. Names in the following are handles used by forum members.

60FlatTop

"My last truck came out at 80% of the MSRP without a lot of monkeying around. It made me happy. (Applied to the CR-V pricing from TrueCar, 80% of the $28,895 MSRP equals a 20% discount [$5,779] and a selling price of $23,116. This means the dealer would take a substantial loss on the transaction *if* the TrueCar factory invoice price of $27,444 was accurate or the dealer paid far less for the car.)

"In 1980 I sold Chevrolets...At that time the margin on new cars was 15% of the sticker price." (15% of the $28,895 CR-V MSRP equals $4,334 or a cost to the dealer of $24,561, almost $3,000 below the TrueCar factory invoice price of $27,444.)

kevin1221

"Our manufacturer gives us 8% percent markup from invoice to MSRP. We do not have holdback, like some manufacturers." (8% markup from the dealer cost of $27,444 equals a margin of $2,196 and a selling price of $29,640 on the CR-V—more than $700 over its MSRP of $28,895.) "Years ago, some manufacturers had 15% to 20% markup. Those days are long over for all manufacturers." (If marked up from the CR-V TrueCar factory invoice of $27,444, 15% equals a margin of $4,117 or a selling price for the CR-V of $31,561; 20% equals a margin of $5,489 or a selling price for the CR-V of $32,933. Both, well above sticker.)

Roger

"To be short: usually the margin for dealers was 19%, less for a cheaper model." (Assuming the margin is based on factory invoice, 19% of $27,444 equals a markup of $5,214 or a selling price of $32,658; again, well above sticker on the CR-V.)

Steve M.

"...the days of 19% markup have long been gone in the US. When I closed my Olds store many models were less than 10%." (10% of the dealer's cost equals a margin of $2,744 and a selling price of $30,188, still above MSRP on the CR-V.)

padgett

"Often...a dealer or zone rep would put 500 miles on and then it was sold as a used car at 25-33% off MSRP." (25% off the $28,895 MSRP equals a selling price of $21,671; 33% off equals a selling price of $19,360. Both well below the purported factory invoice of $27,444.)

Ed

"Yes, 25-33% off a slow selling car with 500 miles is reality."

Steve Mk.

"…new cars are about a wash. Profits come from selling finance, service, and used cars. They are the by-products of the new car sale."

Steve Mz.

"When I got in the business the new car department was the biggest profit center, then it went to the used car department, then it went to the finance department and today many dealers are doing well in the back end (service, parts, and body shop)."

Forum member Frantz mentioned some dealers are publicly traded, multi-location enterprises that issue annual reports, which was news to me. I looked into it and sure enough.

I quickly found an example in Lithia Motors which is headquartered about 40 miles north of the California border in Medford, Oregon. It's a huge company with 92 dealerships spread over 13 states[11] and annual revenues of $8.6 billion.[12]

Lithia's 2015 annual report describes its offerings: "Our Domestic segment is comprised of retail automotive franchises that sell new vehicles manufactured by Chrysler, General Motors and Ford. Our Import segment is comprised of retail automotive franchises that sell new vehicles manufactured primarily by Honda, Toyota, Subaru, Nissan and Volkswagen. Our Luxury segment is comprised of retail automotive franchises that sell new vehicles manufactured primarily by BMW, Mercedes-Benz and Lexus. The franchises in each segment also sell used vehicles, parts and automotive services, and automotive finance and insurance products."[13]

Though automobile "supermarkets" in our era have made multiple-make dealers fairly common, it's still a bit of a shock that a single company is able to sell cars from America's Big Three and a number of foreign manufacturers. In a way, this meshes with the reality that cars from different producers look alike and often are similarly equipped. More than ever they are commodities.

New cars make up 58% of Lithia's auto sales, and used cars, 24.5%. Additional revenues come from auto repair, financing, and insurance sales.[14]

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2015	Revenues	Percent of Total Revenues	Gross Profit	Gross Profit Margin	Percent of Total Gross Profit
New vehicle	$ 4,552,301	57.9%	$ 280,370	6.2%	23.8%
Used vehicle retail	1,927,016	24.5	241,249	12.5	20.5
Used vehicle wholesale	261,530	3.3	4,457	1.7	0.4
Finance and insurance (1)	283,018	3.6	283,018	100.0	24.1
Service, body and parts	738,990	9.4	363,921	49.2	31.0
Fleet and other	101,397	1.3	2,619	2.6	0.2
	$ 7,864,252	100.0%	$ 1,175,634	14.9%	100.0%

The table (above) from Lithia's 2015 report states the "gross profit margin" on new vehicles that year was 6.2%. Retired CPA Paul Matson told me gross profit margin is the difference between what the dealer paid for a car and the selling price; that is, before other expenses are deducted. It's not the actual money made on the car. Presumably that is much less.

Applying Lithia's 2015 GPM to the CR-V indicates if the dealer paid TrueCar's factory invoice cost of $27,444 for the vehicle, a 6.2% margin would be $1,702, and a price to the customer of $29,146, which is about $250 over the MSRP of $28,895. Supported by the Lithia table are often heard assertions that "dealers make the most money on used cars" ("Used vehicle retail" gross profit margin is 12.5%) "and service" ("Service, body, and parts" gross profit margin, 49.2%). The 100% gross profit margin on finance and insurance, my CPA friend told me, probably reflects commissions the dealer received and doesn't include what the insurance costs Lithia.

Although it seems modest, a 6.2% gross profit margin on new vehicles adds up to quite a lot given the number of vehicles dealers sell. Applying it to the average dealer revenue from new car sales of $31 million annually produces a "profit" of $1,922,000. However, this is before expense deductions ranging from advertising to salaries.

Incidentally, googling Lithia popped up a story titled, "Updated: Lithia Motors settles with FTC in nationwide probe into used-car claims."[15] The company's violation was summarized in the lead paragraph: "Lithia Motors Inc. is one of three companies that have settled Federal Trade Commission complaints that alleged the auto dealers failed to disclose some of the used cars they sold were subject to unrepaired safety recalls."[16] Said Jessica Rich, director of the FTC's Bureau of Consumer Protection: "Safety is one of the biggest considerations for consumers shopping for a car. So companies touting the comprehensiveness of their vehicle inspections need to be straight with consumers about safety-related recalls, which can raise major safety concerns." Billions in revenues but still not above shady practices, even ones that might affect the safe operation of vehicles Lithia sells.

It wouldn't surprise 39BuickEight, an AACA member, who posted a comment that reflects poorly on industry practices: "After being a wholesaler for several years, I decided to never enter a car dealership again with the intent of purchasing. Out of the 65 dealers I sold to, two or three might have been honest with their numbers and books. I really don't understand how the manufacturers didn't catch what they did during audits. The stories go on and on, from hiding cars to cooking the books. They would brag about it to me since I wasn't really part of their business. They would ask me to do things that I simply wouldn't do in terms of title and checks. Some wouldn't deal with me because I wouldn't help them play their games. This is mostly related to used cars, but that also included factory sales and dealer trades..."

Revoltingly, dishonesty isn't limited to dealerships but reaches upper management strata at manufacturers; perhaps this is why they aren't always vigilant about policing dealers. In recent years, for example, both Toyota and Volkswagen, Numbers 1 and 2 worldwide,[17] were involved in horrendously unethical, even criminal activities. Volkswagen's troubles were reported in a December, 2017, National Public Radio story posted online:

"High-ranking U.S.-based Volkswagen executive Oliver Schmidt has been sentenced to seven years in prison and ordered to pay a $400,000 fine for his part in a decade-long diesel-emissions cheating scandal...Volkswagen already has admitted guilt to charges of conspiracy to commit wire fraud, customs violations and obstruction of justice, as well as violation of the Clean Air Act. The German company has paid more than $20 billion in fines and settlements."[18]

Toyota's actions and their consequences were summarized by the Australian Broadcasting Corporation in a March, 2014, online story: "Toyota has reached a record $1.32 billion settlement to resolve a criminal investigation into safety issues that have been linked to at least five deaths. The Japanese car maker admitted it misled United States consumers by concealing and making deceptive statements over two safety issues that caused cars to accelerate even as drivers tried to slow them down."[19]

It's shocking that hugely successful Toyota and Volkswagen have corporate cultures that permit such corrupt acts, ones that even lead to customer deaths. Another takeaway is companies able to pay billions in fines and settlements and remain operating obviously make huge profits on every vehicle they produce and sell.

Other automobile manufacturers have been embroiled in their own scandals, and sordid stories are easy to find; probably the worst involved the Ford Pinto of the 1970s. The car's gas tank was prone to rupturing in crashes, causing deadly fires. A National Highway Traffic Safety Administration investigation revealed Ford management knew about the problem but decided it was cheaper to deal with possible lawsuits than redesign the Pinto.[20] Appalling business behavior.

Automaker Nissan made news as I was working on this when its chairman, Carlos Ghosn, was arrested by Tokyo district prosecutors, "…for questioning over allegations of false accounting," stated a Wikipedia article. "Ghosn was taken away for interrogation upon re-entry into Japan on a business jet at Haneda Airport at 4:30 p.m. On the same day, Nissan chief executive Hiroto Saikawa announced at a press conference that Ghosn had been dismissed and would be stripped of executive rights at a meeting to be held November 22. Saikawa stressed that the dismissal was the result of an internal inquiry by Nissan."[21] Wikipedia reported Ghosn is in his sixties, speaks four languages, and made a name for himself at Michelin, where, at age 30, he was appointed COO of the tire giant's South America operations. All that success and still accused of corruption?

Asbury Automotive Group, headquartered about 28 miles northeast of Atlanta, in Duluth, Georgia is the second publicly traded network of dealerships I found online. It has 83 "dealership locations" in "18 metropolitan markets within 10 states" and reported revenue of $5.9 billion in 2014 according to Wikipedia.[22] "As of December 2011, its dealerships represent 30 American, European, and Asian brands," Wikipedia reports.[23] Despite the greater number of dealerships, its annual revenue is about $3 billion less than Lithia's.

The 2015 Asbury annual report lists a "new vehicle gross margin" of 5.6% (see chart below).[24] Applied to the $27,444 factory invoice price on the CR-V this would be a markup of $1,537 for a selling price of $28,981, like Lithia's markup, *above* the MSRP for the CR-V.

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New Vehicle Metrics—

	For the Years Ended December 31, 2015	2014	Increase (Decrease)	% Change
As Reported:				
Revenue per new vehicle sold	$ 34,464	$ 33,806	$ 658	2 %
Gross profit per new vehicle sold	$ 1,915	$ 2,075	$ (160)	(8)%
New vehicle gross margin	5.6%	6.1%	(0.5)%	
Same Store:				
Revenue per new vehicle sold	$ 34,580	$ 33,901	$ 679	2 %
Gross profit per new vehicle sold	$ 1,935	$ 2,086	$ (151)	(7)%
New vehicle gross margin	5.6%	6.2%	(0.6)%	

Asbury's used vehicle gross margin listed in the 2015 annual report was 7.9%[25] and its parts and service gross margin, 62.3%.[26] No gross margin is listed for its finance and insurance products. On page 33 of the report (below), Asbury states sales of new vehicles accounted for 55.4% of its revenue in 2014; used retail vehicles, 26.1%; used vehicles wholesale, 3.3%; finance and insurance, 4%; and parts and service, 11.2%.[27]

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	2015	2014
REVENUE MIX PERCENTAGES:		
New vehicles	55.4 %	55.1 %
Used retail vehicles	26.1 %	26.1 %
Used vehicle wholesale	3.3 %	3.5 %
Parts and service	11.2 %	11.4 %
Finance and insurance, net	4.0 %	3.9 %
Total revenue	100.0 %	100.0 %
GROSS PROFIT MIX PERCENTAGES:		
New vehicles	19.1 %	20.5 %
Used retail vehicles	12.9 %	13.4 %
Used vehicle wholesale	(0.4)%	(0.2)%
Parts and service	43.6 %	42.6 %
Finance and insurance, net	24.8 %	23.7 %
Total gross profit	100.0 %	100.0 %
GROSS PROFIT MARGIN	16.1 %	16.5 %
SG&A EXPENSES AS A PERCENTAGE OF GROSS PROFIT	68.8 %	69.4 %

I'm a born skeptic, but it seems strange that Asbury and Lithia, both giant dealer enterprises, report closely matched revenue percentages but considerably different gross markups for used cars (Lithia 12.5%, Asbury 7.9%) and parts and service (Lithia 49.2%, Asbury 62.3%). Meanwhile their new car gross markups are fairly close (Lithia 6.2%, Asbury 5.6%).

The stated profit margins for new cars published by Asbury and Lithia are far lower than I thought they would be and even below replies I received on the AACA forum where markups experienced by members—some with auto industry experience—ranged from 8% to 33%. Hate to be suspicious, but...

Later I posted a second message in the AACA forum along with the TrueCar CR-V price report: "Thanks for the insightful comments. I invite forum members, who have a little time, to review the attached national sales prices for a Honda CR-V according to TrueCar. The 'market average' is about a grand above factory invoice, some sales appear to be higher than the MSRP and some below factory invoice. Maybe I'm not interpreting this correctly; otherwise, why would a vehicle that sometimes commands more than the MSRP be sold for less than its dealer cost on other occasions?"

This didn't stimulate many responses, but member Frantz opined: "Ummmmmm. Because some people just go in and say yes to whatever offer they get and others negotiate down to get a better deal? For that vehicle $200 under invoice is listed as the 'exceptional' price, the entire spread is less than $2000. Frankly I'd say that's a pretty good position for consumers. Certainly not like stories of the 'good old days.'"

39Buick8 posted: "Dealers sell vehicles below invoice for all sorts of reasons. Favoritism for certain customers (friends, relatives, etc.), but usually they are sold by dealers who focus on one thing—volume. As has been mentioned, dealers can get all sorts of rewards for volume goals...money, preferential cars (like [one] Chevrolet dealer getting more Corvettes than others or Dodge dealers, Vipers [when they were offered]). It is possible to walk into a dealer the last day of any given month, ask which vehicle they need to sell the most, and get a deal that may not be possible otherwise. I would guess, and that's it, a guess, that the CR-Vs sold below invoice also may have had a fantastic trade in the deal. If you are taking a red pickup truck (or similar very highly desirable trade) for a new vehicle and it's a volume-driven dealer, it will move numbers around a lot more. They know they can sell your trade for $xxx, and if you're a real serious customer, they can really adjust things. On the other hand, if your trade is a wholesale piece that they don't even want, they'll still take it, but you're not going to get the same price on the new vehicle. Many different situations can apply to such pricing on new vehicles."

The replies of Frantz and 39Buick8 reinforce my basic opinion that markup in the automobile business is a deep mystery and probably only top-level insiders know what is typical.

Dealerships are high-expense operations with costs of many kinds, from advertising to personnel to paying the utility bills on flood lamp-lighted expanses of asphalt and concrete. After researching this for a while, I still have no idea how the business works. Many aspects seem impossible. For example, how do Asbury and Lithia pay the finance charges on their huge inventories of new vehicles if their *before expenses* markups are a meager 5.6 to 6.2%?

To succeed, I needed to talk with an insider who had dealer and manufacturer experience. "Nick," who wants to remain anonymous, contacted me. Nick's father worked for an automobile dealer, and he followed in his footsteps, starting while a high school student, experienced most dealership positions, then began working for automakers and stayed with them until he retired.

Nick remembers the automobile business fondly but is quick to point out a glaring difference between it and other enterprises: "No product has the situation cars have—customers want to haggle on everything," he said. "A lot of money is tied up in a car all the way around—manufacturer, dealer, consumer—so that makes for a much bigger decision than buying a refrigerator. Car dealerships go through a lot of cash."

Moreover, Nick knows customers, their expectations, and craftiness. "They'll say, 'Give me your lowest price,' but then they don't trust what the salesperson says. Instead, they'll want to bargain *down* from there." Certainly salespeople know this and are reluctant to supply a "lowest" price. On it goes...

Manufacturers don't like negotiating on price and have tried to reduce it but face two giant obstacles. "Some cars sell readily without much discounting," Nick said. "In the 1970s after the OPEC oil embargo, fuel-efficient Japanese cars were in high demand so dealers tacked on a surcharge that they listed as ADP, which stood for 'additional dealer profit.' Customers paid full MSRP *plus* ADP. American cars meanwhile, which weren't engineered for low-gas consumption, were tough to sell and needed to be discounted deeply. 'Gotta find an ass for every seat,'" Nick reflected, "is an industry saying."

And one I found in *The Dictionary of Modern Proverbs*: "We have a term here [at a car dealership], 'There's an ass for every seat.' Once in a while you get a car that's ugly...It's a car that you think, oh my gosh, nobody's ever going to buy that one. And sure enough, somebody'll come in and say, 'just what I've always wanted.'"[28]

Second obstacle is the trade-in, which never seems worth as much to the dealer as the customer thinks it should be given the price it will be listed for on the used lot. Nick said trade-ins are often tough for dealers, too. "Cash flow issues at dealerships are really challenging and customers don't care," he began. "Say a dealer sells a car for $30,000 and gives the customer $15,000 for a trade-in. If the dealer paid the OEM $27,000 for the new car, there's a net loss of $12,000 until the used car sells—it's a tough business."

When I told Nick I had looked at two large, publicly traded dealers, he said I should review three more: AutoNation, Penske, and Sonic.

Wikipedia calls AutoNation "...the largest automotive retailer in the United States..."[29] The firm's annual report indicates it sells 35 different brands including the Big Three; Volkswagen; Honda, Nissan, and Toyota; Hyundai; and others ranging from Fiat to "smart" (small "s" is the way the company lists its name and AutoNation refers to it as smart in its report).[30] Revenue is $21.6 billion[31]; company headquarters, in Fort Lauderdale.

AutoNation's 2016 annual report states new vehicles were 56.7% of revenues, used vehicles 23.1%; finance and insurance, 4.1%; and parts and service, 15.4%. Also listed is "other" at 0.7%.[32]

Penske, with headquarters in Bloomfield Hills, Michigan, has revenue of $17.2 billion.[33] According to its 2016 annual report, new vehicles were 51% of revenues; used vehicles, 30%; finance and insurance, 3%; and service and parts, 10%. Also listed is "fleet and wholesale," 0.7%.[34] The company sells all major brands with BMW and Mini generating 25% of revenue, Audi, 14%, and the Big Three only 4%.[35]

In Sonic's 2016 annual report, new vehicles—it sells all major brands—are listed as producing 54% of revenues; used vehicles, 28%; finance, insurance, and other 3%; and fixed operations ("sales of replacement parts and performance of vehicle maintenance, manufacturer warranty repairs, and paint and collision repair services") 15%.[36] Sonic sells imports primarily; Big Three brands contribute just 12.8% to its revenue.[37] Surprisingly, BMW at 21.8%, accounts for more Sonic sales than any other brand.[38]

According to their annual reports, gross *new* car profits were: AutoNation, 19.2%[39]; Penske, 7.7%[40]; and Sonic, 18%[41]. Gross *used* car profits were: AutoNation, 23.1%; Penske, 30%; and Sonic, 28%.

New car gross profit figures in the cases of AutoNation (19.2%) and Sonic (18%) are about three times higher than what Asbury (5.6%) and Lithia (6.2%) reported. Penske is similar at 7.7%. Why the difference? It would seem from plain statistics all five would be within in a point or two of one another; Lithia and Asbury are .6 apart and AutoNation and Sonic a little more than one point apart, but the spread between high and low is 13.6%.

The table below compares the published markup expressed as gross profit (what Nick calls "margin") of the five publicly traded companies along with its impact on selling prices. If other factors weren't involved and a dealer actually paid the TrueCar factory invoice price of $27,444, each of the selling prices would exceed the CR-V's MSRP of $28,895.

Company	Reported New Vehicle % Gross Profit	Gross Profit % added to TrueCar Honda CR-V factory invoice of $27,444	Selling Price with Gross Profit as listed in annual reports added to the TrueCar factory invoice (MSRP for the CR-V is $28,895.)
Asbury	5.6	+1,537	$28,981
AutoNation	19.2	+5,269	$32,713
Lithia	6.2	+1,702	$29,146
Penske	7.7	+2,113	$29,557
Sonic	18	+4,940	$32,384

In the case of the CR-V pricing, the table is strong evidence that dealers typically do not pay what TrueCar represents as "factory invoice." In addition, and to my surprise, Nick related that TrueCar, the pricing service I was referred to by *Consumer Reports* is not what it seems. Its *primary* business is supplying leads to auto dealers.

A recent article in The Detroit Bureau, an online news outlet that calls itself "the voice of the automotive world," reported: "Most auto pricing services are built around a referral, or lead, model. Their goal is to get website visitors to click on a dealer link. Each time that happens they get paid. TrueCar only makes money, however, when someone actually purchases a vehicle."[42]

As mentioned earlier, when I began working on this article, I tried to get a printout (as I had in the past) on a car so I would have fresh, so-called dealer and factory invoice prices. Visiting the *Consumer Reports* website, I interacted through chat:

“Some years ago I ordered printouts from *Consumer Reports* that specified MSRP and factory invoice prices as a means of negotiating to purchase a new car. Are these still available?”

CR: “Thank you for waiting. We value you as a customer and would like to help quickly with your request. You are now chatting with Jason. Hi, Ted. Please give me a moment to look up your account. Thank you for your patience.

“OK.”

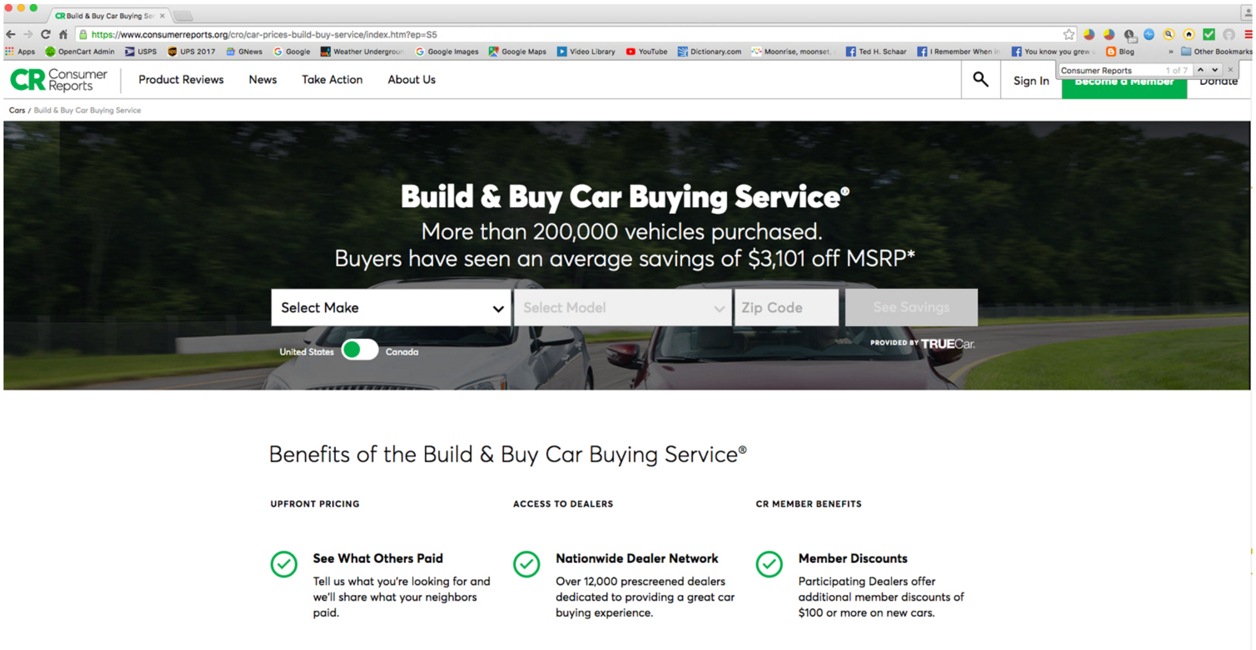
CR: “I apologize, Ted, unfortunately, this service has been discontinued.”

“Do you know when and why it was discontinued?”

CR: “It was discontinued April 2016 due to low customer demand. We have a similar service that you might find helpful. I have attached a link[43] below for you.

The link took me to the “Build & Buy Car Buying Service” which I didn’t realize at the time was operated by TrueCar.

The screen capture below shows the top of the opening screen at the link; the *CR* logo in the upper left corner is much larger and more prominent than the rather subtle "Powered By TrueCar" graphic which is located just below pulldown menus for "Select Make" and "Select Model" and a blank for zip code.



Scrolling way to the bottom, a block of small type appears in an area the magazine itself might characterize as the normal home for "explanations" that take the wind out of inflated claims punctuated by a "pesky" asterisk: "The *Consumer Reports* Build & Buy Car Buying Service…is provided to *Consumer Reports* users by TrueCar.com. TrueCar operates the Service's dealer network and the Service's website. *Consumer Reports* collects a fee from TrueCar for vehicles purchased from a TrueCar Dealer. 100% of the fees we collect goes to support our nonprofit mission. *Consumer Reports* has no financial relationship with any dealer."

Initially, I didn't see the small print. When I did, it seemed completely un-*Consumer Reports*-like to me. From my decades of reading and often subscribing to the magazine, *CR* made a point of keeping as far away from businesses whose products it reported on as it possibly could. In the pages of the magazine I remember writers pointing out that items were purchased anonymously so there wouldn't be any special prepping to make sure CR got a particularly good example. Now the company appeared to be in cahoots with the automobile industry. Huh?!?

I decided to make sure I was understanding this correctly, looked online, and identified two *CR* public relations specialists. My first inquiry went to both. An associate director of communications replied with language similar to what was in the small print.

Follow-up questions elicited careful answers which, again, shocked me. Completely out of character with the always transparent, objective *CR* I knew and loved.

I sent him the quote from the Detroit Bureau article[44] cited earlier and queried: "Does *CR* view TrueCar as *primarily* a lead generation service?" His boilerplate reply didn't answer the question.

Looking to learn more about the history of the program, I asked when it began and how much *CR* has collected in fees to date. He answered it began in 2010; in reference to fees, he stated: "CR's revenue from TrueCar is a proprietary matter; no matter what the number, all the fees we collect goes to support our nonprofit mission."

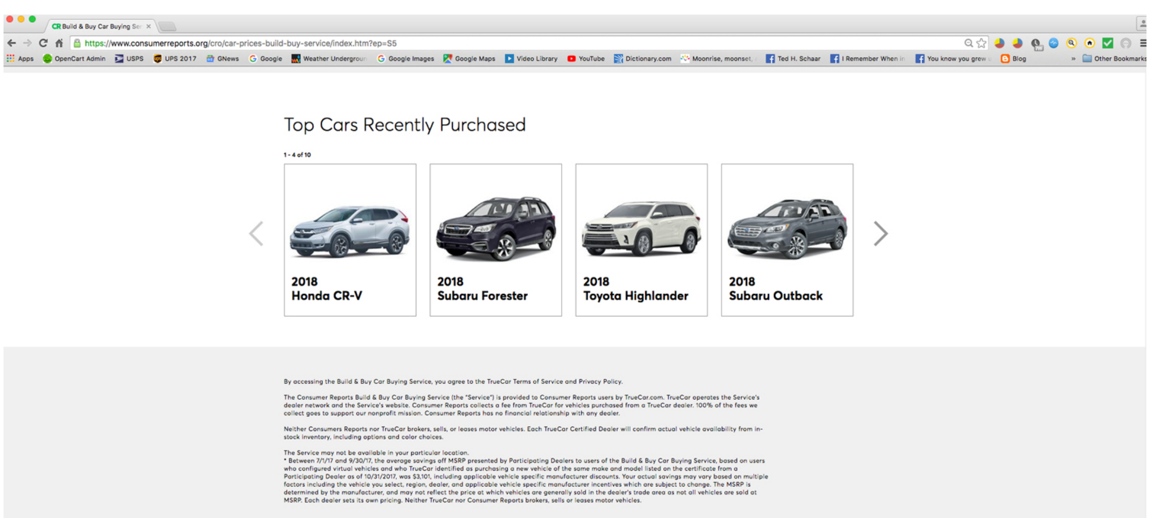
I decided to see if *CR* had annual reports, and soon found myself reviewing the latest published on September 30, 2018.[45]

On page 9, three categories of products are listed under "Nature of Goods and Services": "Digital Products, Print Products, and Other Revenue." The third appears to be where earnings from the relationship with TrueCar are listed:

> Other revenue primarily consists of referral fees received from a contract with a 3rd party to remit a portion of revenue based on consummated transactions by customers directed to their products from our digital products. This category also contains revenue associated with the licensing of CR's content. Other revenue is typically recognized at a point in time when delivery of the content to the customer occurs, or the referral fees are earned based on the date of the underlying sale.

Once again, the above is rather cagily put. According to a statement on page 10, "Other revenue" accounts for $10,502,000 of the $206,553,000 total—just 5% of the total but still a sizable amount of money.

Reviewing the report, I was set back a bit by how successful an enterprise *CR* is. On top of $206 million in revenue it also received $28 million in financial gifts or contributions during the reporting period:[46]



"Your gift to Consumer Reports helps save lives and makes everyday life better because it supports our work throughout the year: testing, rating, and reviewing thousands of products and services; creating more than 2,000 articles and 400 videos that engage and inform; speaking up on consumer issues; and advocating for rules and regulations that keep you and your family safe."[47]

I was further surprised to learn *CR* also "partners" with Cars.com, Amazon, and eBay.[48]

Trying to nail down when these relationships began brought more unexpected *CR* evasiveness mainly through non-responsiveness. After receiving no reply to a question e-mailed on August 23, I sent follow-up inquiries a week and two weeks later to no avail.

The day after the third went out, I e-mailed an inquiry to the other *CR* e-mail address I had, mentioning my first contact's failure to reply and asking whether he had left the company. Almost immediately I received a bounce-back announcing the recipient (not my first contact) *had left* CR and stating I could contact his manager. An e-mail to the manager produced an immediate reply stating he (the manager) was away from the office and advising contacting the staff member (my first contact) who was unresponsive and evidently *still* with the company. This is rational, down-to-earth *Consumer Report*s?

The next morning an e-mail from the manager appeared. Rather than answer my weeks-old question, which was included in my message, the manager asked, "What is the focus of your story?"

After my, "The retail automobile business…" reply, nearly a month after I asked what I thought was a straightforward question, the answer came:

"Apologies again for the delayed response. *CR* launched a partnership with eBay Commerce Network in 2013, with Amazon in 2014, and with Cars.com 2016. You should have all of the information you're seeking."

Despite the presumptuous final line, I asked why my original contact ignored me and why it took so long to get an answer. The response was in character with the goofiness I was used to from *CR* staff: "…I apologize, but your request fell through the cracks. When you reached out to someone else, it got passed on to me. I've provided you with the answers to your questions."

More presumption; hard to believe.

Conclusion? *CR* is embarrassed by these relationships because, after all, they are signs the organization, which always prided itself on objectivity, has ventured in the direction of financial convenience. Ah, money! It'll do that and of course the car business floats on an ocean of cash.

Another aspect insider Nick helped me appreciate is the phoniness of the figure TrueCar—and through its relationship, *CR*—represents as "factory invoice." He explained relatively normal discounts dealers receive proving this line from my original AACA post correct: "No, I don't believe dealers pay anything near what is listed on the 'factory invoice,'"; some members thought it unfriendly toward the industry, my conversations with Nick soon confirmed it was simply a fact. According to him, dealers typically pay only 93% of the MSRP to put vehicles on their lots. Applied to the 2017 CR-V example, 93% is $572 below the TrueCar-reported factory invoice cost of $27,444 (MSRP is $28,895). And that's just for starters.

"Another 3% of MSRP is holdback—almost everyone uses this," he continued. "It's a way of preventing dealers from *giving too much away*, because to make the sale, some give *all* the net profit away; holdback is paid quarterly and might be thought of as 'mom holds some back.'" "Net" profit means more than gross because it factors in dealer expenses ranging from advertising costs to property taxes and includes salaries and expenses for office furniture and so on.[49] Nick said net profit usually ranges from 2 to 4%. On typical dealer sales of $31 million per year this means pure profit of between $620 thousand and $1.2 million.

More net profit can be made by cutting costs for billing, invoicing, personnel, and so on. Additionally, dealers often make money on real estate according to Nick. They buy and occupy desirable land on the outskirts and then sell after the city limits have moved farther from the center of town and their properties are enveloped.

Overall, dealers try to achieve or better the targeted upper net profit number of 4%, proceeds that presumably go to owners or benefit stockholders.

So now we're down to 90% of the CR-V's $28,895 MSRP or a cost to the dealer of $26,005 which is $1,439 below TrueCar's factory invoice cost of $27,444.
(I should note, as a lawyer might [and I've worked with some] that the term "factory invoice" doesn't necessarily mean a whole lot. It doesn't, for example, proclaim itself to account for exactly what a dealer pays. It's just the *factory invoice*. It might appear to be the price paid, but appearances are often deceiving.)

Another 2.5% discount off the MSRP is available for four or five different things, Nick continued. "Examples are achieving a good CSI (customer service index) rating—if the dealer meets the standard, he or she earns X amount. Additional earnings are available if other manufacturer standards are met. Most dealers have a 'sales efficiency' standard in their 'areas of responsibility' and 'areas of influence'; basically each dealer is responsible for market penetration and rewarded for achieving it. There are 50 sets of rules, one for each state."

Dealers, according to Nick, aim to make a total gross profit of 12.5% on each car sold. Applying this to the $28,895 MSRP of the 2016 Honda CR-V puts the dealer's actual cost at $25,283, $3,612 off the MSRP and $2,161 below TrueCar's factory invoice cost of $27,444.

Some of it helps pay two of three kinds of advertising expenses, Nick said: "Tier 1 ads appear across the nation, are financed by manufacturers, and proclaim, one way or another, 'This is the best car ever!' Tier 2 ads are regional, 'Hot summer event! Buy now!' Tier 2 costs are shared by dealers who sell the line of cars promoted in certain areas; Tier 3 is dealer-specific advertising such as, 'Visit Cape Chevrolet Sales And Service.' Each dealer is responsible for shouldering its cost."

Most manufacturers also offer "market support," Nick said, in the form of "floor-plan assistance"—a payment for each new car the dealer stocks to help cover the cost of loan interest. Some cars sell quicker, and interest rates right now are fairly good; "floor-plan interest was killing dealers in the '70s," he recalled.

In addition, Carmakers put "special money" in the form of customer rebates on some cars to help market them. "But," Nick said, "rebates create the image that a car is undesirable and won't have good resale value. Some manufacturers refer to rebates as 'money in the trunk or on the hood.' I've seen it go as high as $10,000 on expensive cars. Rebates are fairly simple—what's complex are plans that go by various names, including 'stair-step programs' and 'volume incentives.'"

Jeremy Anwyl, writing in *Edmunds,* sketches how such programs work: "As sales increase, the incentive amounts increase as well. For example, dealers might earn $500 per unit if they sell 10 units over the course of the program, $750 if they hit 15, and $1,000 if they hit 20 units. Often there will be a fast-start bonus as well. There is a more aggressive version of a stair-step program and that is when the incentives are paid retroactively. This means that if a dealer hits the first tier, the $500 would be earned for units 1-14, not just 10-14. As you can see, one aspect of stair-step programs is that they can get very complex very quickly.[50]

Nick says many dealers hate stair step; others discount more deeply anticipating stair-step income that might not materialize.

Mark Scarpelli, 2017 National Automobile Dealers Association chairman and principal of Raymond Chevrolet and Kia in Antioch, Illinois, in a May 18, 2017, *Bulletin of the Chicago Automobile Trade Association* essay wrote:

"There is an elephant in the room when it comes to the retail auto industry, and it's named 'stair-step incentive programs,' particularly the unfair and indiscriminate kind. We all know how the elephant was born: automakers rolled out dealer incentive programs in the form of escalating bonuses if sales targets were achieved. The OEMs' intention was straightforward enough: to provide dealers with a carrot to sell harder and push more and, consequently, wrest back market share or boost key models. These programs are inherently tied to the modern dealership business. The programs were all a novel incentive, or so we thought."[51]

Scarpelli's characterization of the program as designed to "...provide dealers with a carrot to sell harder and push more..." is emblematic of the aggressive selling attitudes that permeate the automobile business, not just at dealers but up the line to manufacturer executive suites.

"And as many dealers have expressed," Scarpelli continues a few paragraphs later, "some programs are not available to everyone, so dealerships of a different size or those in a different location can be at an extreme disadvantage compared to the dealerships that utilize these programs.

"There is no doubt that auto retailers all want a healthy outcome: dealerships brimming with sales and happy customers and moving inventory. But at what cost? I am asking our OEMs, 'How many of the gains are you really willing to offset through counterproductive methods that move us back to where we started?' If these programs run afoul of everything our customers care about—trust, fairness, and transparency—then it's not really worth it anymore.

"When these programs are implemented, they often negatively affect our businesses, the value of our brands, and our collective integrity. Moreover, these programs that lead to multi-tier pricing have a tendency to be more disruptive to the marketplace than beneficial. Most important, we know for a fact that they're incredibly detrimental to the customer experience and our customers' trust in the brand."[52]

Mike Jackson, who runs Auto Nation and is described as a "brilliant guy" by Nick, "hates step steps," Nick said, "because dealers anticipate getting the number and discount on that basis, selling at a price closer to what they pay for the car and pressuring other dealers to follow along."

A 2016 NADA survey found that "64 percent of respondents said stair-step incentives disrupt the market and often hurt credibility."[53]

Mitch Walters, president of Friendship Family of Dealerships in Bristol, Tennessee, is quoted in an *Automotive News* article titled, "Worry grows as stair-steps get steeper": "It's kind of tough for the customer sometimes because at the end of the month, you make them a deal that's reflective of a stair-step program and if they decide not to buy, they think that price carries forward to the next month, but you may not be able to make that price."[54]

Asbury Automotive Group Inc. COO David Hult said Asbury is going back and forth on whether to pursue stair-step targets. Hult noted that "some of the domestics" have changed their programs this spring and summer [2016] and reduced the amount of money being dangled as an incentive.[55]

The situation is much different from 2015, observed Asbury CEO Craig Monaghan: "Last year, there wasn't a month that we didn't have the attitude that we're going to chase it and try to get it. This year, it's been far more of a topic, and it's really been month by month."[56]

Another surprising, even *bewildering* area of income for dealers is the "floor-plan assistance" Nick mentioned. Dealers currently are able to *make money* off the help manufacturers provide in terms of financing the inventory of new cars they have on their showroom floors and in their parking lots.

Jim Henry writes in *AutoNews*: "How did this cost become a profit source? For now, low interest rates make it affordable for automakers to provide substantial floor-plan support, to motivate dealerships to buy more inventory, Szakaly said. By taking advantage of that support, generally by turning inventory quickly, dealerships can come out ahead on their floor-plan costs"[57]*—an understatement of monumental proportion!* For example, Henry reports AutoNation's 2015 "new-vehicle floor-plan interest expense was $55.3 million," but it received "$117.8 million in floor-plan assistance." Lithia Motors' "interest expense of $19.5 million was offset by $41.4 million in floor-plan assistance." Meanwhile, Asbury cleared $17.5 million and Sonic, $21 million, all due to floor-plan assistance.[58]

Smaller operations benefit, too, according to Henry, with the average dealership receiving about $110,000 in revenue through floor planning, enough to provide a revenue gain of about $143 per vehicle retailed.[59]

If a dealer is able to sell the CR-V for its MSRP of $28,895 and take advantage of all the discounts Nick mentioned, her or his gross profit on the sale would be $4,655, about a 16% overall margin. The dealer's actual cost in this example is $3,204 below TrueCar's reported factory invoice of $27,444. See table below.

Summary of Possible Dealer Discounts

	Honda CR-V 2017 MSRP $28,895	Amount below MSRP	Amount below TrueCar Factory Invoice $27,444
-7% (amount off MSRP dealers pay) (-$2,023)	$26,872	-$2,023	-$572
-3% holdback (-$867)	$26,005	-$2,890	-$1,439
-2.5% for a good customer service index rating and similar factors (-$722)	$25,283	-$3,612	-$2,161
Possible stair-step incentives, $250 to $1,000	-$500 = $25,283 -$1,000 = $24,383	-$3,862 -$4,512	-$2,661 -$3,061
Possible floor-plan revenue	$143	$4,655	-$3,204

Lowest identified[*] possible cost of 2017 Honda CR-V to dealer	$24,240 (assumes $1,000 stair-step incentive)	-$4,655 below MSRP	-$3,204 below TrueCar factory invoice (assumes $1,000 stair-step incentive)

AACA forum member Todd C. steered me in a new direction when he posted: "I am a commercial/fleet manager at a Ford & Chrysler dealer group and previously worked for a Chevy/Olds/Nissan dealer. The holdback is usually 3% from Ford/GM/Chrysler paid monthly or quarterly into an account by the automaker...the Internet means dealers have more similar pricing on cars than ever, since it is so easy to compare. The 50-100% markups may indeed still be the starting point in furniture or jewelry but car dealers are more like grocery stores—maintaining large facilities and staff hoping to make 3-5% if people buy a few extras. In fact I often joke that now new cars are like grocery store bananas for 39 cents a pound. You know the store can't be making money at that price but they use that 39-cent banana special to get you in the door and hope you buy more stuff."

I'd accept this if dealers had anything approaching the volume of grocery stores. I visit a supermarket once a week, generally spending upwards of $100, and there's usually a line in every checkout aisle. I almost never visit automobile dealerships. To find out more about grocery industry markups, It struck me some food chains might be publicly traded like vehicle dealerships, so I did a Google search and sure enough, Kroger is.

"The Kroger Company, or simply Kroger," Wikipedia reports, "is an American retailing company founded by Bernard Kroger in 1883 in Cincinnati, Ohio. It is the United States' largest supermarket chain by revenue ($109.83 billion for fiscal year 2016), the second-largest general retailer (behind Walmart), and the twenty-third largest company in the United States. Kroger is also the third-largest retailer in the world. As of December 2015, Kroger operates, either directly or through its subsidiaries, 2,778 supermarkets..."

Kroger is more than five times larger in terms of revenue than AutoNation, the country's biggest dealer organization. The table below reports sales of $115 billion and operating profit of $3.4 billion.

Kroger 2016 Annual Report
page A-30

(In millions, except per share amounts)	2016 (52 weeks)	2015 (52 weeks)	2014 (52 weeks)
Sales	$ 115,337	$ 109,830	$ 108,465
Merchandise costs, including advertising, warehousing, and transportation, excluding items shown separately below	89,502	85,496	85,512
Operating, general and administrative	19,178	17,946	17,161
Rent	881	723	707
Depreciation and amortization	2,340	2,089	1,948
Operating profit	3,436	3,576	3,137
Interest expense	522	482	488
Earnings before income tax expense	2,914	3,094	2,649
Income tax expense	957	1,045	902
Net earnings including noncontrolling interests	1,957	2,049	1,747
Net earnings (loss) attributable to noncontrolling interests	(18)	10	19
Net earnings attributable to The Kroger Co.	$ 1,975	$ 2,039	$ 1,728
Net earnings attributable to The Kroger Co. per basic common share	$ 2.08	$ 2.09	$ 1.74
Average number of common shares used in basic calculation	942	966	981
Net earnings attributable to The Kroger Co. per diluted common share	$ 2.05	$ 2.06	$ 1.72
Average number of common shares used in diluted calculation	958	980	993
Dividends declared per common share	$ 0.465	$ 0.408	$ 0.350

[*]There might be discounts beyond these that potentially lower the dealer cost even more.

Doing a percentage calculation (dividing sales by operating profit) indicates an overall margin of approximately 2.9%. However, unlike the margins Asbury and Lithia report, this amount is *after* deducting expenses such as "...advertising, warehousing, and transportation..." and "operating, general, and administrative" costs which Investopedia states are things like, "...building rent, executives wages and benefits, depreciation on office fixtures and equipment, and insurance, as well as legal counsel salaries, various office supplies, accounting and tax fees, legal fees, and electricity and water bills."[60]

The following table shows that about 70% of Kroger's revenue is from typical grocery sales and the rest from fuel and pharmacy products. That there is only about a 3% difference between reported profits from Kroger, Asbury, and Lithia is remarkable given how different their products are. Again, it's hard not be suspicious...but perhaps I simply am not understanding how the process truly works and my skepticism is unwarranted.

On the other hand, in an industry where the number one and number two sellers of vehicles were found guilty of costly—billions in fines and settlements were paid—even deadly crimes, anything is possible.

Kroger 2016 Annual Report
page A-40

	2016		2015		2014	
	Amount	% of total	Amount	% of total	Amount	% of total
Non Perishable (1)	$ 60,220	52.2 %	$ 57,187	52.1 %	$ 54,392	50.1 %
Perishable (2)	27,666	24.0 %	25,726	23.4 %	24,178	22.3 %
Fuel	13,979	12.1 %	14,802	13.5 %	18,850	17.4 %
Pharmacy	10,432	9.0 %	9,778	8.9 %	9,032	8.3 %
Other (3)	3,040	2.7 %	2,337	2.1 %	2,013	1.9 %
Total Sales and other revenue	$ 115,337	100 %	$ 109,830	100 %	$ 108,465	100 %

(1) Consists primarily of grocery, general merchandise, health and beauty care and natural foods.
(2) Consists primarily of produce, floral, meat, seafood, deli, bakery and fresh prepared.
(3) Consists primarily of sales related to jewelry stores, food production plants to outside customers, data analytic services, variable interest entities, specialty pharmacy, in-store health clinics, digital coupon services and online sales by Vitacost.com.

I've been researching and writing this story off and on for more than two years and am still mystified and sometimes, *flabbergasted*—a word I rarely use.

The latest perplexing reality is how AutoNation, a giant corporate enterprise, receives $117.8 million in floor-plan assistance from manufacturers of brands it sells when its floor-plan interest expense is "only" $55.3 million (bankers have to love these guys!). That's more than a 100% markup! And evidently "compensation" such as this—automaker to dealer—is not uncommon.

Nick shed some light when he explained floor-plan assistance started in the late 1970s during a period of high interest rates and was designed to make it easier for dealers to stock cars. Since then loan rates have fallen dramatically though occasionally they rise; when they are high it's more of a break-even situation for dealers than what exists currently. Asked why manufacturers don't simply say to dealers, "Send a monthly report on the amount you pay to finance stocking our vehicles, and we'll send a check," Nick replied that would be disastrous during periods of high interest.

Another source of wonder is the fierce competitiveness for each ass; it's blatant, unusual, off-putting, often rude. I don't experience it with other kinds of purchases or businesses; I don't understand why it seems endemic to the automobile industry.

Case in point. Coincidental to my work on this, my wife decided to purchase a new car and narrowed the choice to models from two different manufacturers. We visited dealers for each on a Thursday night, and she test drove vehicles she was interested in. I accompanied her because she was nervous about going alone, but I stayed out of the decision-making process.

Both salesmen (M and H) were friendly and knowledgeable though H was a bit more aggressive. H checked her trade-in and said it appeared to be in good condition. M said he would e-mail pricing the next day and did; H called the next morning as he said he would, however, he was vague about pricing and told Pam his manager would need to see her trade-in before a value was assigned. Pam said she was babysitting our grandchildren and couldn't visit again until about 7:00 p.m. Friday night. She wanted me to go along so I did. The purpose of the visit as she understood it was to have the sales manager assess the value of her car.

I told her this was strictly a ruse and H and his manager would probably lean hard on us to do the deal on the spot. We arrived on schedule and H was at the reception desk just inside the showroom; he was all smiles and invited us to his desk—a simple table with a few chairs.

He remained friendly until we made it clear that we were only staying for as long as it took to have the sales manager assess the car. He asked why, and I told him we had somewhere to go. "Where?" he said. Forward of him, I thought, and not his business—so I said "dinner." He then said he had waited "four hours" for us to arrive and clearly wasn't happy. By now, his sales manager had spent maybe five minutes, if that, looking at the car. The manager's appraisal was the same as H's.

H started putting together numbers. I told him he could e-mail them to us the next day; no, he said, he wanted to do it while we waited. In the process, he opined Pam's trade-in needed new rear tires which she found hard to believe because she had all four replaced 16 months earlier.

Pam wasn't sure of the color she wanted and asked H if there was another model on the showroom floor with a shade of red she liked. He said no, it was only available on the model she was interested in. When she asked if a model with that color was on the dealer parking lot, he said we should look to the south of the showroom. He didn't take us out to find one and didn't offer to shake our hands when we parted. The next day my wife bought a car from M who was far less pushy, and who, with no prompting, proclaimed her tires to be in good condition.

What a creepy experience we had with H, and what a neat summation of what the industry does to some people. In his defense, H probably is paid little or nothing if customers don't buy a vehicle and so is highly motivated to sell, even if it means stretching the truth.

That's a shame.

Thanks to Nick I've come to appreciate different discounts dealers receive off MSRP and why conventional wisdom recommending "buying toward the end of the month" is often good advice.

But I have a lot more to learn. If you have industry experience and want to contribute anonymously, like Nick, or let it all hang out, please write ted@tswrites.com.

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