



Financial Management Objective Homework

**Student
Class #**

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Name:

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Academy

I plan to accomplish the following objective by our next class on:

June 4, 2018

Implementation of the certified used vehicle program. Measurement will begin at the end of the month of May.

Provide the relevant composite data

Department	Month	Page	Column
Used vehicle dept. profit center 8.65%	March	18	5B
Inventory (pre-owned) vehicle turns 9.52	March	6	8B

Action plan for achieving objective
<p>What is the area of focus?</p> <p>The pre-owned vehicle department's gross return on investment ("GROI") for Georgetown Honda ("GTH") is currently 82.35%. The NADA Guide would suggest the GROI for this department should approximate 144%. GTH has a negative variance of 61.65% or 42.8% of the NADA Guide.</p> <p>I'm focusing on the pre-owned department and</p>

GROI for two reasons. Firstly, GTH's variance from the NADA Guide is simply too large to ignore and secondly the metric is too important to ignore. Simply put, GTH is in business to generate an acceptable GROI in all our departments. GTH's pre-owned vehicle department has contributed roughly 16% of the total sales year-to-date, but less than 13% of the gross profit. The pre-owned department is having a significant impact on the operating profit of the business, unfortunately that impact is negative through 10 months (operating loss of \$61,280).

A department's GROI measures all the operational elements of that business. By extension, generating a strong GROI (usually established based on the expectations of the equity investors or on established rules of thumb) should be the focus of every automotive dealer.

Based on the composite data observed, I will focus solely on the GROI in our pre-owned vehicle department. Pre-owned GROI has two major components, which are equally relevant and which will both be dealt with in turn; average YTD gross as a % of sales and pre-owned vehicle inventory turns.

GROI is the factor of gross margin percentage and inventory turns.

1. Average YTD gross (pre-owned) as a % of sales (Page 18, 5B)

BOC Honda	13.06 %
NADA Guide	12.00 %
Group Average	8.93%
<i>GTH</i>	8.65%

2. Pre-owned vehicle inventory turns (Page 6, 8B)

			*		
NADA Guide	1 2	÷	1.0 0	=	12.0 0
<i>GTH</i>	1 2	÷	1.2 6	=	9.52
BOC Honda	1 2	÷	1.5 0	=	8.00
Group Average	1 2	÷	1.5 0	=	8.00

* month's supply of pre-owned vehicle inventory

GTH's pre-owned vehicle department's GROI = 8.65% x 9.52 = 82.348%

If GTH were singularly able to increase our gross profit percentage to the NADA Guide, an additional \$142,131 of gross margin would be generated (3.35% of YTD sales of \$3,535,606 x (12/10)) on an annual basis.

If GTH were singularly able to increase our used inventory turns to the NADA Guide (at our existing pre-owned vehicle margin of 8.65%), an additional \$385,499 of gross margin would be generated (YTD sales 3,535,606/9.52*12*0.0865).

If GTH were dually able to increase its gross profit percentage and used inventory turns to the NADA Guide, an additional \$641,757 of gross margin would be generated (YTD sales 3,535,606/9.52*12*0.12), which is obviously a greater total than the sum of the individual parts as a greater margin percentage is being applied to a higher turning pre-owned inventory.

It will be difficult to increase both the gross margin percentage and the pre-owned inventory turns simultaneously. The focus of this plan will be to increase one or the other, or a combination of both to increase the pre-owned vehicle department's gross margin by \$195,514 and its GROI by 49.6%.

What is the proposed plan? How will you achieve it?

The expected outcome of the plan is twofold; increase the margins in GTH's used vehicle department from 8.65% to 11.00% while increasing the number of retail units from 144 to 200 (39% increase).

These are both "stretch" goals (or WIG), but I feel they will be achievable through the re-introduction of the "Honda Certified Used Retail" program at GTH. Beginning in April 2018 GTH has reintroduced the certification of used cars in line with Honda's National certification program. Based on the financial forecast that I've assembled, I expect that the certification program may have the impact of increasing margins in the used car department by approximately 2.35%.

Summary	Current	Forecast	Change	%
Pre-owned (units) annual	144	200	56	39%
Average sale price	\$ 11,746	\$ 12,885	\$ 1,139	10%
Total gross profit - non-certified used	\$ 302,216	\$ 465,167	\$ 162,951	54%
Total gross profit - non-certified used (annualized)	\$ 362,659	\$ 558,200	\$ 195,541	54%
Gross profit (per unit)	\$ 2,472	\$ 2,791	\$ 319	13%
Month's supply of pre-owned inventory	1.24	1.00	-0.24	-20%
Gross profit percentage	8.65%	11.00%	2.34%	27%

The certification program will help drive sales growth and lead to a price enhancement for used vehicles. Honda Canada estimates that simply providing a certified used program would increase year-over-year sales by 10-15%. Pairing the certification program with other Honda enticements, such as financing packages, trade-in offers, etc... could be expected to double this for GTH. I have modeled a 39% increase in this case to hit 200 units (annualized) for the following 12-month period beginning June 1, 2018.

The certification program will increase the average cost of a used vehicle by \$900 to \$1,200. That represents an approximately 7.6% to 10.2% increase. Some of the new costs will include vehicle servicing (\$600/unit) and manufacturer charges

(\$289/vehicle). The increase will also incorporate a margin enhancement.

It is important to note that this plan will not only impact the used car department, but service as well. I have not modeled the increased gross margins from service in the used car department (obviously), but notionally one should include this gross margin when evaluating the merits of the certification program on the dealership. Based on GTH's service gross profit margin of 70%, certification of approximately 200 vehicles could be expected generate additional gross margin of \$84,000 in the service department.

	Current		Forecast		
		per unit		per unit	Notes
Pre-owned inventory (current)	\$	415,044	\$	452,631	
Pre-owned inventory (units)	\$	33	\$	33	
Average value of pre-owned inventory		\$ 12,577		\$ 13,716	1
Total sales (10 months)	\$	3,535,606	\$	4,273,595.30	\$ 12,885
Gross profit - non-certified used	\$	201,703	\$ 1,681	\$ 333,333	\$ 2,000
Gross profit - non-certified used (F&I)	\$	94,933	\$ 791	\$ 131,833	\$ 791
Gross profit - wholesale	\$	5,580	\$	5,580	
Total gross profit - non-certified used	\$	302,216	\$ 2,472	\$ 465,167	\$ 2,791
Cost of sales	\$	3,333,903	\$	4,526,310	
Average COS	\$	333,390	\$	452,631	
Month's supply of pre-owned inventory		1.24		1.00	
Wholesale (units)		181		181	
Retail used units sold to date		120		167	
Annual projection - retail (units)		144		200	
Total used department gross profit	\$	302,216	\$	465,167	
Total used department sales	\$	3,492,006	\$	4,229,995	
Gross profit percentage		8.65%		11.00%	

Notes

- Per unit sales will increase based on the following:

Additional service charges - Honda certified	\$	600
Manufacturer charges	\$	289
Margin enhancement	\$	250.0
	\$	1,139

The plan will require the sales manager and sales staff to aggressively acquire Honda vehicles via trades and other methods and then turn these vehicles over at a faster rate than previously with the non-certified vehicles. An incremental sales incentive program will be implemented to entice a suitable level of attention from the staff to the certified used Honda vehicles.

In modeling this department, wholesale vehicle sales have been held constant. The gross margin contribution from used wholesale sales is nominal.

How will you track your progress? What measurements, KPI's? How often will you track?

Progress will be tracked notionally on a continuous basis, in accordance with the regular new and used vehicle sales updates which occur daily.

Detailed calculations will be conducted monthly based on the dealer statements. The KPI's will include many different elements, the details of which can be found

in the supporting Excel schedule (attached), but will focus mainly on the following:

1. Gross profit % (per unit);
2. Average sales value (per unit);
3. Sales, certified used (units) - growth;
4. Total gross profit, certified used;
5. Total (incremental) gross profit, service;
6. Inventory turns, certified used; and
7. Used department GROI.

Who are the employees that will be involved, or impacted? Will they require training or assistance?

The employees in the sales department are key to the success of the plan. On a secondary basis, the service department will be impacted through a greater volume of certified used vehicles. The sales department will be instrumental in the success of the plan. Their involvement will ensure the following:

1. Obtain sufficient inventory of used Honda's, appropriate for certification;
2. Turn the inventory of certified used Honda's (approximately 17/month) to achieve the annual goal of 200 units;
3. Articulate the advantages of the Certification Program to the customers to educate them on the benefits associated with certification (and the associated vehicle cost);
4. Focus on the value enhancement associated with certification to boost the gross margin percentage in the used vehicle department from 8.65% to 11.0% (modeled).

Honda Canada provides some free online training to the sales staff on the certification program. We will ensure that all sales staff have successfully completed this online course. The service department does not necessarily need additional training to provide certification on these vehicles. They will ensure that the vehicles are inspected and serviced in accordance with the program details provided by Honda Canada.

Is there a cost, or estimated cost for implementation?

Upon vehicle registration, fees of \$289 per passenger vehicle and a \$329 per truck/SUV/minivan will be payable. These registration fees have been modeled into the vehicle's cost. Additional charges include a \$250/month administration fee payable by GTH. The monthly administration fee is being waived by Honda Canada until October 2018. Some other (nominal) additional charges may include curbside advertising, or other promotions associated with the program (e.g.: emails to customers).

It is expected that the gross margin percentage realized by the service department will remain unchanged with the (slightly) higher volume of work associated with the certification of these vehicles.

Projected date of completion? May 31, 2019

Jan.	Feb.	March	April	May	June
July	Aug.	Sept.	Oct.	Nov.	Dec.