# Investing in Car Dealerships: How to Do It Right

**By John Pico, BA, JD**

**Article Word Count:** 1324

The financial characteristics of the automobile dealership are attractive:

> . . . moderate growth and risk and high returns. Franchised new car dealer revenues have grown at a 7.2% annual rate since 1992, about twice the rate of GDP. Moreover, this growth has come with only moderate risk, as the dealer body didn't lose money (on a pretax basis) for a single year in the last twenty even during the 1989-1991 industry down-cycle. Finally, despite major changes in the auto industry's structure, dealer returns have remained high, with pretax ROE averaging 26.1% over the last twenty years. [MerrillLynch, April 19th, 2004 Report on Automobile Dealers.]

Athletes from almost every major sport have invested in new car dealerships: Rick Hendrick, Roger Penske, John Elway, Troy Aikman, Evander Holyfield, Arnold Palmer, Michael Jordan, Scottie Pippen and Alex Rodriguez to name a few.

The idea isn't new. Johnny Lujack, 1947 Heisman Trophy winner and Chicago Bear Pro-Bower, started a business in 1954 that would eventually expand to 16 franchises; spread over 40 acres, with sales of over 10,000 vehicles and $150 million, per year. Lujack retired from the auto business after almost 50 years as a successful dealer.



## WHEN IS THE RIGHT TIME?

"This is the time you have been waiting for", reports Greg Gilmore in the June 2005 issue of Dealer Magazine. Dealer Executive reported that last year (2004) ranked as the 4th best for new unit sales by franchised new-vehicle dealers. Total dealership dollars exceeded $714 billion, up more than 2% from 2003.

The fact is that anytime is the right time. In 1991, in the depths of an automotive depression, John Elway asked me, prior to signing his purchase contract, if this (1991) was the right time to buy. I told him that it is how you buy it and how you sell it that count. That year he made a $20 million investment. At the time he had a single Mazda store on Arapahoe Road, in

Englewood. I sold the Mazda franchise for him and Nissan gave him its franchise to put in the old Mazda building. Shortly thereafter, I put together another transaction that had John buy the Mazda store on 104th Avenue, in Thornton. John then terminated Suzuki and put the Mazda store with his Oldsmobile and Hyundai franchises. After that he bought one more dealership (a Ford franchise) and then, in 1995, sold the entire package to Republic Industries for $86 million.

A lot of people were afraid to buy a dealership in 1991 and thought that John took a big gamble. But, he didn't gamble. He structured his purchases and sales correctly, and then capitalized on his investment.

For example, although GM and Ford lost money (as they did in 1991), individual dealers made millions, according to NADA (National Automobile Dealers Association) and Automotive News statistics, the average dealers pretax margin varies between one and two percent of their total sales. Why? The dealers capture a broader business base than the manufacturer. While the manufacturer makes its money on new car sales, the dealers have the additional balance of the parts departments, service departments, used car departments, finance departments, insurance departments and, in some instances, body shops. Consequently, while the manufacturer is dependent upon each year's new car sales, a dealer's success is based more on the total number of vehicles in operation.

## DOES THE DEALERSHIP'S HISTORY MATTER?

A little, but don't be intimidated by it. After Jimmy Vasser won the CART racing championship for Target, I put together a transaction for Jimmy to buy a dueled Chevrolet-Toyota franchise, in Napa, that lost money for the previous 10 consecutive years. I put Jimmy together with a dealership manager and Jimmy's dad, who had some previous used car experience, signed-on as used car manager.

Subsequently, after going to dealer school and passing through the chairs, Jimmy's dad took over as General Manager; the store thrived; and Jimmy not only bought the dealership land and facility, but bought the Ford store in the next town, and is currently building a new Toyota store so that his Chevrolet and Toyota franchises can have separate facilities.

## WHAT DOES IT TAKE TO BE SUCCESSFUL?

Good advice. Good advice is both important and hard to find. In the words of Trace Armstrong, past president of the NFL Players Association: There's just so much bad advice out there being given to these guys. It's really kind of scary. [Reported by Eric Fisher, March 27, 2000.]

As with the Entertainment and Sports Industries, there is so much money in the car business, that everybody wants to get a piece of it. Consequently, everybody thinks he or she is an expert in analyzing and structuring deals, when in fact they just want to be a broker that gets a commission from the deal. Sidebar: New car dealership revenues reached almost One Trillion Dollars in 2004. The dealerships and dealer related industries account of over 15% of the Gross National Product of the United States.

## HOW TO CREATE A SUCCESSFUL TEAM?

An investor needs a team. Generally, it's the same team they have, supplemented by an expert in the car business. Don't get lulled into a false sense of security that loyalty is synonymous with the factory or bankers☐.

For example, Ford made one of its black dealers (a superstar athlete) the point man, brokering meetings with senior executives and acting as a conduit between the company and Jesse Jackson. He mediated disputes between Ford and its dealers, and he promoted the company in public appearances. He even had a close relationship with some Ford family members.

"He had some friends in high places," said John Clissold, a retired Ford Credit executive. "[The head of Ford Credit] was a very strong supporter." But, when trouble came, it didn't matter. Business was business. . . . one factory executive familiar with the situation summed up the prevailing feeling at corporate headquarters: [the superstar] was headed for a cliff and we weren't going over with him. [Story by Bill Vlasic and Mark Truby / The Detroit News Sunday, May 26, 2002.]

The fact is that the factory and bank employees have a duty to do what is best for the factory or bank, not what is best for your client. It's the law. They have a legal obligation to their shareholders no matter how nice or how close your client is to them.

Financial statements and an accountant are not enough. Your client needs a member of your team that is a student of the industry. A profitable automotive statement can be certified and comply with every principle of accounting, yet still convey a false impression of success. There are so many nuisances in defining and structuring automotive transactions, that your client needs an expert in the field who can determine both what automotive deal is best for the athlete and what is the best way to get it.

So while your team may consist of accountant, attorneys, agents and managers that are excellent at their jobs, unless a student of the industry is added (someone who does nothing but structure buys and sells everyday), a key ingredient to success will be missing.

Think of it in terms of any sport or business. If a person wants to create a championship team in a particular sport, is it created with people who play the game 50% of the time, 75% of the time, or someone who plays it every day?

Remember: The nicest thing they ever said about Richard Nixon was: "He looks like a used car salesman."

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Starting in 1972, Pico entered the automobile business by representing dealership groups such as Tasha Corporation (once the 17th largest dealer group in the country before it sold to AutoNation), and handling sales such as Lucy DiGulio's sale of her deceased husband's share of Prospect Motors (currently the largest General Motors dealership in the nation) to Skip Halverson.

Before retiring from the active practice of law in 1980 Mr. Pico and his law firm represented numerous automotive dealers in the reorganizations, purchases, and sales of dealerships. He both tried cases as the attorney for the dealerships and arbitrated and mediated dealer related cases.

Mr. Pico built upon his experiences and became a student of the industry by receiving training and attending seminars with respect to the various departments in new car dealerships, participating in National Automobile Dealer Association (NADA) Management Education Program, having "hands-on "experience" operating a store by filling in as General Manager on an "interim" bases. In 1986, after five years of research and two years of writing, Mr. Pico authored and National Legal Publishing Company published the nation’s first book on Buying and Selling Automobile Dealerships.

Mr. Pico is recognized as an expert in the field of buying, selling and investing in automobile dealerships. In addition, both State and Federal Courts have also recognized Mr. Pico’s expertise and in various legal proceedings he has been:

- Approved by the U.S. Bankruptcy Court, 10th Circuit</b>, District of Colorado, pursuant to Rule 202 of the Bankruptcy Code, as "Consultant to Debtor" in sale of a new car automobile dealership;
- Approved by the U.S. Bankruptcy Court, 9th Circuit</b>, Northern District of California, pursuant to Rule 202 of the Bankruptcy Code, as "Consultant to Debtor" in sale of a new car automobile dealership;
- Approved by the U.S. District Court, 8th Circuit</b>, Wisconsin, as Arbitrator/ Appraiser in new car Dealership litigation;
- Approved by the District Court of Colorado</b> as expert in dealership valuation litigation;
- Approved by the Superior Court of California</b> as :(a) “Consultant to Court Appointed Receiver" in check-kiting case,(b) "Expert Witness", with respect to dealership valuations, and(c) Superior Court Mediator in dealership/lender litigation.