Residual Based Financing

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How can Dealers lead in the growing opportunities of the Certified Pre-Owned Market?

According to Yen Chen, senior economist at the Center for Automotive Research in Ann Arbor, Michigan, while car sales are climbing steadily, they are still depressed by a lack of full-time jobs for young adults. Consumers aged 25 to 34 whom are typically the likely sources of additional sales has been declining as the number of them with only part-time jobs continues, even as older workers retire. These consumers may not be able to afford a new car but they can certainly buy a certified pre-owned vehicle with the same level of service as a new car. A study by Autobytel and Polk in 2014 found that nearly 46% of consumers who planned to buy a new vehicle bought a used car or truck instead. To the Dealership, this is the best time for them to take assisting the cars buyers to get the vehicles they desire and can afford.

Certified Pre-Owned (CPO) – "The New Normal"

The advent of CPO Programs was in the late 90's when the off-lease volume acutely increased. The goal of the manufacturers was to preserve residual values during a period when the primary focus was on selling new cars rather than used. In 2014, new car lease penetration was at its highest level since post 2008. Lease penetration will continue to grow in 2015. The uncertain state of the economy also makes CPO attractive with benefits pitched to consumers including multi-point inspections, extended warranty coverage, and value relative to a new vehicle – in essence, consumers were purchasing a superior used vehicle. In addition, the consumer can avoid the high up-front 20 to 40 percent depreciation cost the original new-car buyer suffered in the first two to three years of ownership. Hence, it is no surprise that CPO sales today represent about 19% of all franchised dealers used-vehicle sales and is becoming an integral part of a dealership's used-car department according to Edmunds.com. Tom Webb, Manheim's chief economist, said he believes that certified used-vehicle sales will reach 2.5 million this year 2015, equal to the number of off-lease vehicles expected to return to the market.

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The Financing Dilemma

In the uncertain economy, financing has also gotten tougher and payments are higher. In order to keep monthly payments low, the average finance term is drawn out over 60 months. In fact, the average terms hit 66 months and is continuing to rise. According to Experian, loans with terms extending out 73 to 84 months made up 24.9% of all new-vehicle loans originated during the quarter, growing 27.6% since the first quarter of 2014.

Statistics show that the average consumer is looking to trade in their current vehicle after 26 months into a 60 month contract. This scenario creates an in-equity position for the consumer and a lost customer for the dealer. They do not return to the originating dealer for a couple of basic reasons:

- They know they owe more for the car than it's worth; and
- They do not want to return to the same store due to embarrassment or they blame original dealer for their current predicament.

In a way, it is a "lose-lose" situation for both the dealers and the consumers. Unless, you create a new way; a better way.

Residual Based Financing with Certified Pre-Owned Program (RBF/CPO)

A solution for consideration is the use of ***RBF/CPO.*** How does the ***RBF/CPO*** strategy works? The premise of the program is to introduce a 24 or 36 month balloon finance alternative to the conventional retail instalment contract focuses on the two most important buying needs of today's consumer of a) Low monthly payment and b) Trade cycle management (allowing the consumer to trade out of vehicle much faster).

With ***RBF/CPO***, CPO buyers will experience a "walk away" balloon payment contract with payments up to 40 percent less than conventional financing payments. In comparison to residuals at 38-60 percent offered to dealers from new vehicle leasing, pre-owned residuals on certain make/model vehicles can run from 45-85 percent. The key to this offer is that the depreciation of a vehicle was consumed

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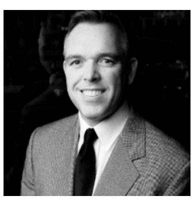
by the first ownership; the 24-month residual approximates its current wholesale value. That translates into a trifecta of gains:

- The dealership maintains customer loyalty and continual trade cycles while still profiting;
- The consumer has affordable payments in a vehicle they desire with a likelihood of decreasing ownership time for continual upgrade; and
- The financer gains business through dealerships by offering the program that benefits its members.

As the auto industry continues to set strides of recovery, ***RBF/CPO*** Strategy is set with one main objective – to satisfy a new opportunity that puts buyers into the cars they want and allow dealerships the possibility of offering more selection and receive the residuals needed to grow and thrive. This is the best time for dealerships to take advantage of the market unfolding before them.



Rob Mudd, CEO at SmartCast Global – Integrated Media Executive & Speaker

For more than 20 years, Rob (Robert) Mudd has been integral in implementing revolutionary advertising solutions for thousands of Mudd Advertising clients nationwide. Rob worked his way through every position in the family business and became the lead speaker in the automotive advertising space for the business and remains a loyal ambassador as a Board Member to Mudd Advertising

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