

MAXIMIZING SESAME STREET AUTO GROUP'S PROFITS

Prepared for
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Owner and Chief Executive Officer
Sesame Street Auto Group, Inc.

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April 21, 2014

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MEMORANDUM

TO: Big Bird, Owner and Chief Executive Officer

FROM: Dewey Cheatham, Finance Manager

DATE: April 11, 2014

SUBJECT: Maximizing Sesame Street Auto Group's Profits

Here is the report that you requested last month on Sesame Street Auto Group's used car sales.

As I mentioned, we are purchasing many vehicles that we cannot sell. It seems as if the ultimate reason has been because we simply want to make all of our customers happy. Sure, customer satisfaction plays a huge role in creating a good reputation for our dealership, but it cannot be the sole reason as to why we purchase certain cars. Our purchases exceed the number of cars we sell, therefore, the dealership is losing money.

The solution is simple: we need to stop purchasing cars that are not in high demand, and instead, focus on vehicles that are popular among customers. Also, the current cars on our lot that we have not sold within a year, we have to market them at a promotional price in order to break even. If this does not work, as a last resort, we can sell them to other dealerships.

These vehicles are depreciating in value every month. Which means, that for every month that we cannot sell a car, we are losing money.

I am thankful for Quack Car and Four Wheel Auto's willingness to provide their inventory information for the last three years. Without their help, I would not be able to tell where Sesame Street Auto Group ranks locally.

Thank you for allowing me to work on this project. I have learned more about our company's spending and I am eager to begin the process of making more money. Please feel free to give me a call if you have any questions or concerns.

EXECUTIVE SUMMARY/ REMOVED for CLASS PURPOSES

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MAXIMIZING SESAME STREET AUTO GROUP'S PROFITS

Introduction

Sesame Street Auto Group has always provided great quality used vehicles for customers at reasonable prices. To make sure that all customers always receive the best service, the dealership offers a variety of vehicles to choose from. Although this method has been appropriate for customer satisfaction, there are several vehicles in our inventory that we are not selling. Last year, Sesame Street Auto Group lost over half million dollars by purchasing vehicles that are still sitting in the lot. This year, and all of the years to follow, Sesame Street Auto Group will maximize its profits by specializing in vehicles that are most popular amongst customers. The dealership will sell mainly "hot cars" that most customers are looking for.

Purpose, Scope, and Limitations

The purpose of this report is to analyze the amount of money the dealership spends on vehicles every year, and to cross reference that amount with the types of vehicles sold within the last three years. This will paint a picture of which types of cars customers are looking for, and which ones are the most and least popular amongst our clientele. Although this will only give the dealership a general idea of which types of vehicles to sell and not to sell, the exact financial influence of these actions is hard to predict. This is an outline of what Sesame Street Auto Group's profits could be should we carry out these measures.

Sources and Methods

In preparing this report, I analyzed the dealership's annual vehicle purchases. I then compared the vehicles in our lot to Wall St. Cheat Sheet's *America's 10 Most Popular Cars*. I also used our personal records and statistics to see which types of vehicles customers purchased most often. I cross referenced this data with our inventory for the entire year to see which cars were popular and which ones were difficult to sell. I used the data from two other used car dealerships within a ten mile radius and examined their inventories based on their website. All of this information allowed me to estimate how much money Sesame Street Auto Group is spending on vehicles that we cannot sell, because there is not a high demand for them. I created alternate options that we can take to maximize our profits by only spending money on vehicles we know will sell.

Report Organization

This review describes the types of cars purchased by Sesame Street Auto Group, which vehicles have highest demand, and steps to making the most possible profit by meeting the demands of our customers.

THE HIGH COST OF VEHICLES

Although Sesame Street Auto Group purchases vehicles at great deals, that does not mean they are cheap. Last year, the dealership spent an annual average of \$1,782,000.00 for vehicles purchased, not including any repairs that had to be done to the cars. In return, these generated a gross income of \$2,872,779.00, which makes the profit \$1,090,779. Note that these figures are just the purchase and selling of vehicles, and do not include any other sales the dealership made such as car repairs or warranties.

Profits Could Be Higher

Last year, Sesame Street Auto Group purchased 264 vehicles, with the average purchase price being \$6,750.00 per car. Out of these 264 purchased vehicles, the dealership only sold 221, at an average selling price of \$12,999.00 per car.

The forty three vehicles that were not sold cost the company an estimated out of pocket expense of \$290,250.00. This could have been a potential gross profit of \$268,707.00.

Demand for Vehicles

As the finance manager of Sesame Street Auto Group, I personally see the types of vehicles that customers are seeking. In today's economy, customers are seeking reliable family vehicles with good gas mileage, a high safety rating, and low maintenance. According to Wall St. Cheat Sheet's *America's 10 Most Popular Used Cars*, the following vehicles are the most highly demanded vehicles in America, in order from most popular to least popular, and followed by the overall percentage of used car sales for that particular vehicle:

1. Honda Accord (2.3%)
2. Toyota Camry (2.2%)
3. Nissan Altima (2.0%)
4. Honda Civic (1.9%)
5. Ford F-150 (1.8%)
6. BMW 3-series (1.8%)
7. Toyota Corolla (1.6%)
8. Chevrolet Impala (1.3%)
9. Chevrolet Malibu (1.1%)
10. Ford Escape (1.1%)

The top four of this list were our top four "hot cars." Out of the 67 Toyota vehicles that were sold by Sesame Street Auto Group last year, 46 were Camry's. Of the 41 Honda vehicles sold, 27 were Accord's and 11 were Civic's. The dealership also sold 18 Nissan cars, 15 of which were Altima's. All of these vehicles meet the basic criteria customers seek when purchasing a car.

Purchased vs. Sold Vehicles

In the previous year, there is no doubt that the dealership made a decent profit. However, what the dealership did not do to its full potential, is meet the customer's demands. There were a number of cars that the dealership bought but never sold, we gave some back to auctions while majority of the cars remain parked on the lot.

Figure 1 illustrates the number of cars (by brand) that Sesame Street Auto Group sold in 2013, while Figure 2 illustrates the number of vehicles (by brand) that the dealership purchased in 2013.

Figure 1 , Sesame Street Auto Group- Number of Cars (by Brand) Sold in 2013

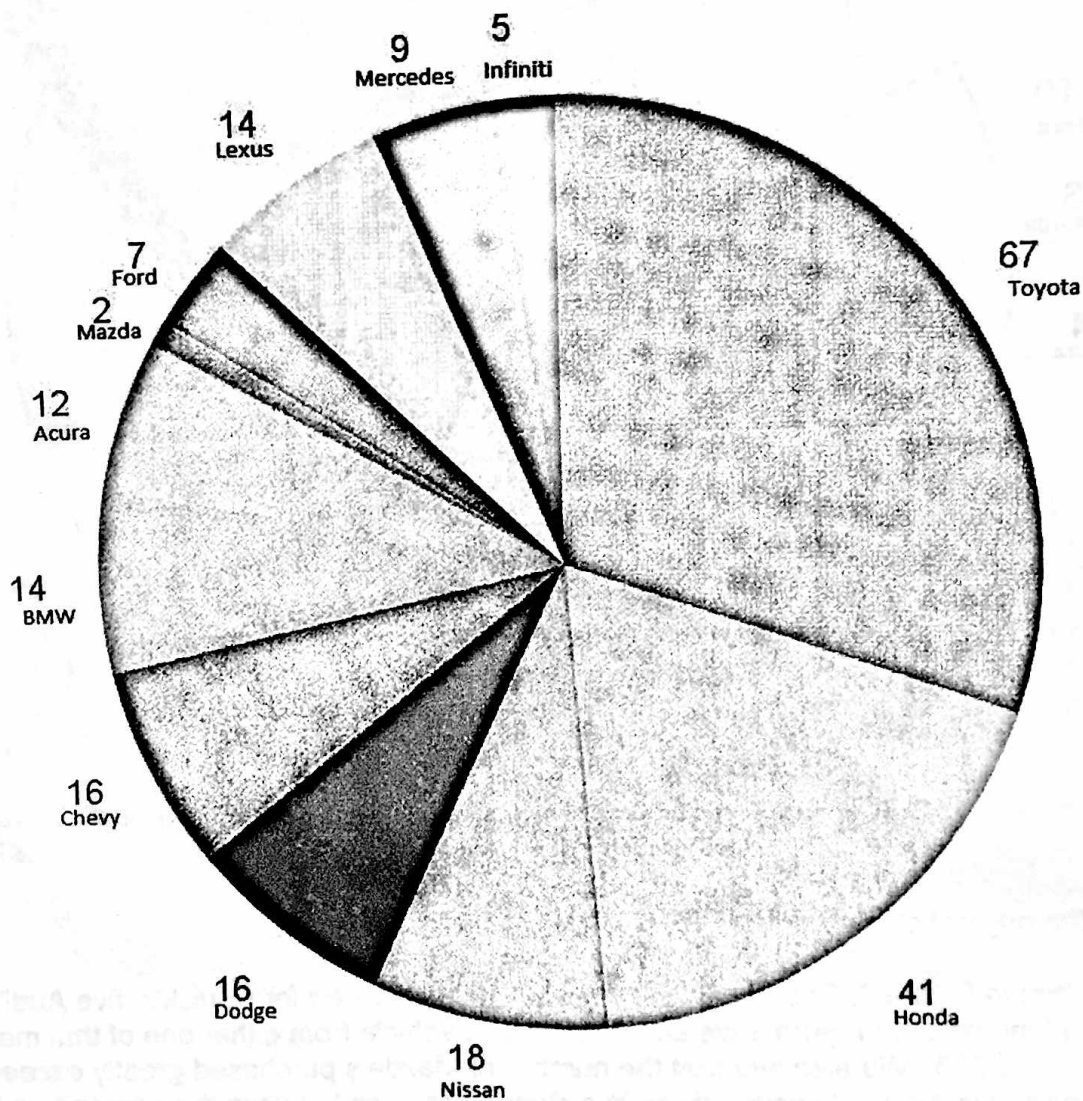
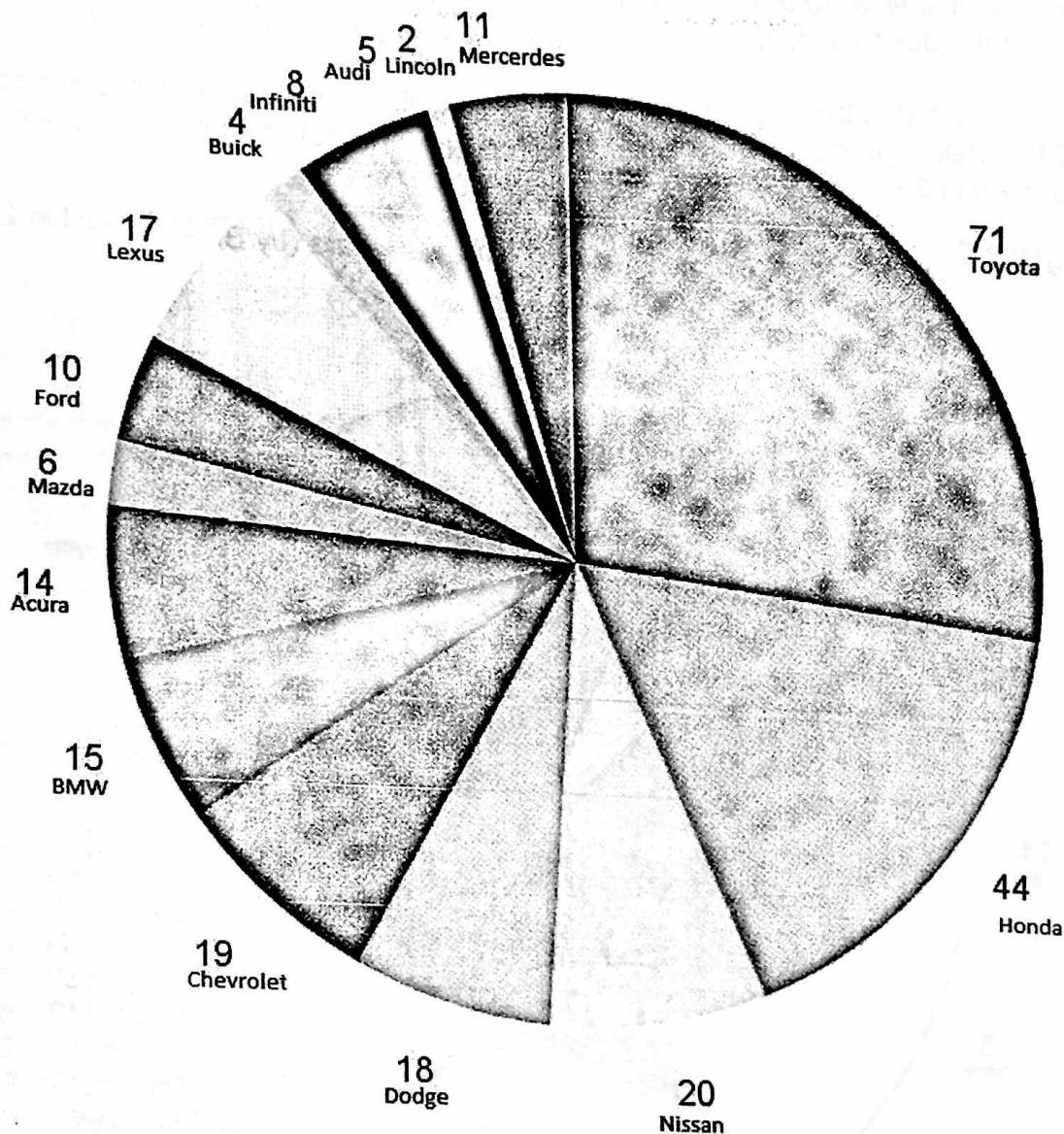


Figure 2 Sesame Street Auto Group- Number of Cars
(by Brand) Purchased in 2013



[note-the original chart is color-coded]

Notice that in Figure 2, Sesame Street Auto Group purchased four Buick's, five Audi's, and two Lincoln's. In Figure 1 we see that not one vehicle from either one of that make was sold in 2013. We also see that the number of Mazda's purchased greatly exceeds the demand for them. However, there is a clear correlation between the demand and supply for "hot cars."

Table 1 is a difference chart of exactly how many vehicles Sesame Street Auto Group purchased versus the ones sold. It illustrates both pie charts combines.

Table 1

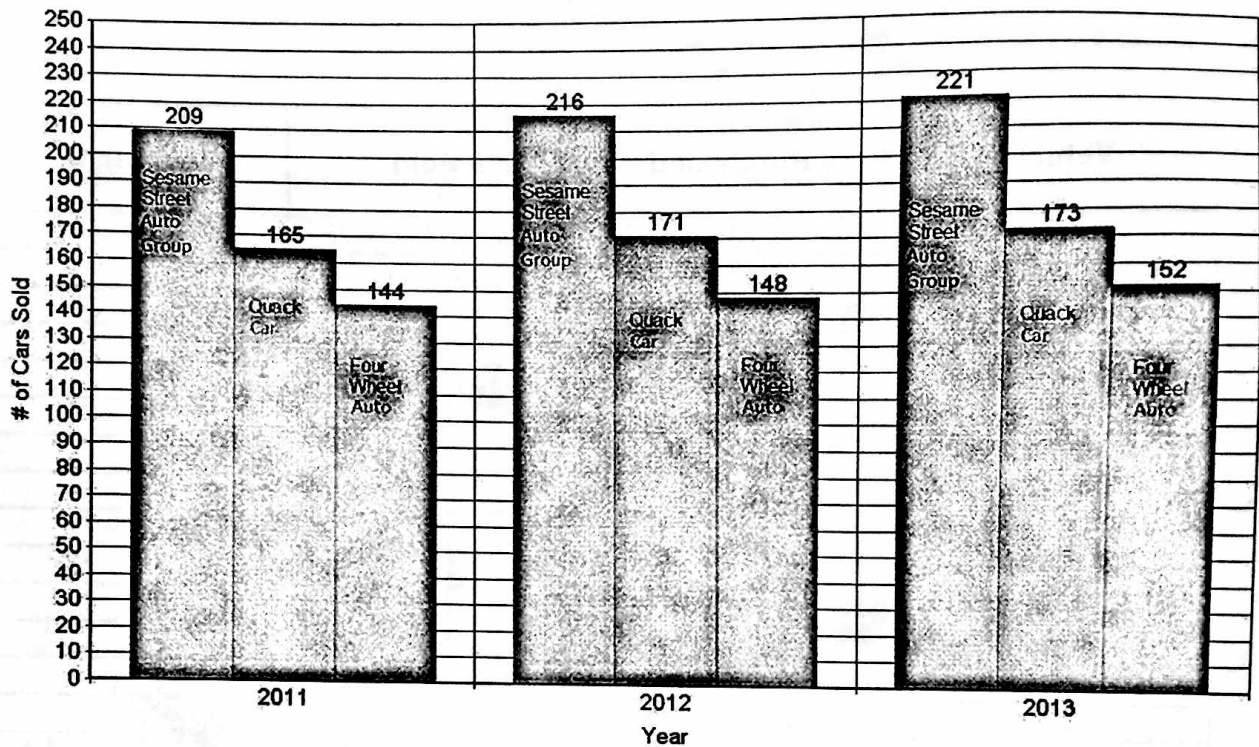
Vehicle	# Purchased	# Sold	Difference
Toyota	71	67	4
Honda	44	41	3
Nissan	20	18	2
Dodge	18	16	2
Chevrolet	19	16	3
BMW	15	14	1
Acura	14	12	2
Mazda	6	2	4
Ford	10	7	3
Lexus	17	14	3
Buick	4	0	4
Infiniti	8	5	3
Audi	5	0	5
Lincoln	2	0	2
Mercedes	11	9	2

Other Dealerships

I compared two other car dealerships to Sesame Street Auto Group. Sesame Street Auto Group ranks first in number of vehicle sales for the last three years, Quack Car ranks second, and Four Wheel Auto ranks third. Based on the data I recovered from the dealerships themselves as well as their online websites, overall, the number of sales is rapidly increasing each year for each dealership. Although Sesame Street Auto Group does rank first, its competitors follow closely behind and continue to increase their number of sales each year.

Figure 3 illustrates the number of vehicles sold by each dealership in 2011, 2012, and 2013.

Figure 3

Top 3 Dealership
Number of Vehicle Sales

[note original chart is color-coded]

The main reason why Sesame Street Auto Group ranks first is because of the customer satisfaction. The dealership has been providing services for customers for over ten years. Many of the customers are repeat customers, while others are referrals, walk-in customers, etc.

Even though our customer satisfaction is rated well, the purchase to sell ratio can improve. Based off of Quack Car's and Four Wheel Auto's online inventory, they are making the same mistake as we are, only on a larger scale. In order to continue being the number one used car dealership within our location, we cannot keep buying cars we cannot sell. Instead, we have to focus of which cars sell fastest and are the most common sells.

Just like Figure 3 illustrated the amount of vehicles sold within the last three years for the dealerships, Table 1 shows the total number purchased versus the number sold. The graph table also shows the average purchase price and selling price of the vehicles for that year, along with the average gross potential lost profit.

Table 2

2011			
DEALERSHIP	CARS BOUGHT	CARS SOLD	DIFFERENCE
Sesame Street Auto Group	249 (avg: \$7,250 per car)	209 (avg: \$10,900 per car)	40 (potential lost profit: \$146,000)
Quack Car	232 (avg: \$7,330 per car)	165 (avg: \$10,300 per car)	67 (potential lost profit: \$198,990)
Four Wheel Auto	197 (avg: \$7,560 per car)	144 (avg: \$9,950 per car)	53 (potential lost profit: \$126,670)

2012			
DEALERSHIP	CARS BOUGHT	CARS SOLD	DIFFERENCE
Sesame Street Auto Group	258 (avg: \$6,998 per car)	216 (avg: \$11,550 per car)	42 (potential lost profit: \$191,184)
Quack Car	240 (avg: \$7,245 per car)	171 (avg: \$10,999 per car)	69 (potential lost profit: \$259,026)
Four Wheel Auto	201 (avg: \$7,300 per car)	148 (avg: \$10,399 per car)	53 (potential lost profit: \$164,247)

2013			
DEALERSHIP	CARS BOUGHT	CARS SOLD	DIFFERENCE
Sesame Street Auto Group	264 (avg: \$6,750 per car)	221 (avg: \$12,999 per car)	43 (potential lost profit: \$268,707)
Quack Car	239 (avg: \$7,100 per car)	173 (avg: \$13,100 per car)	66 (potential lost profit: \$369,000)
Four Wheel Auto	215 (avg: \$7,250 per car)	152 (avg: \$13,400 per car)	63 (potential lost profit: \$387,450)

As you can see in the "difference" column, we are losing way too much gross profit per year, and the other two dealerships are losing even more. Yes, we have a greater number of cars sold throughout the years, but that does not mean that we cannot make more money. There is a fierce competition in this area among these dealerships, and we cannot afford to lose any more money on vehicles that are not in high demand. This is money that can be going into our pockets. Instead, it is just a loss that the dealership is not doing anything about.

Just like Sesame Street Auto Group, the other dealerships also purchased vehicles that do not meet the demands of the customers. Many of these vehicles are similar to the ones that we cannot sell, such as Buick, Lincoln, and Mazda.

METHODS TO DECREASE SPENDING AND INCREASE PROFITS

By lowering the amount of money the dealership spends on vehicles that customers tend to not look for and investing in vehicles that are popular and trending, Sesame Street Auto Group can maximize its profits.

Four Ways to Make More Money

1. Stop buying cars that are obviously not selling. If customers are not looking for these types of vehicles, we should not be carrying them in stock. Purchasing cars that nobody is seeking is a waste of money and space on the dealership's lot. If Sesame Street Auto Group stop buying these types of cars, there will be more room for other cars that are easier and more common to sell.
2. Begin taking requests. As I am well aware, there are instances where customers come in seeking a vehicle and the dealership does not have it. So, the customer goes to different car dealerships in search of their dream car. Instead of buying unnecessary vehicles that we cannot sell just to try to make us look as if we have a bigger variety, the dealership can take requests. Since Sesame Street Auto Group buys vehicles from various sources, such as auctions, other dealers, and private parties, there is a good chance that we can often times find the vehicle that the customer is seeking.

Ask the customer exactly what type of car he or she is searching for: the year, make, model, color, mileage, and price range. Search for that type of vehicle in the databases before purchasing it. Let the customer know once you have found it. If the customer is still serious about that vehicle, have him or her put down the total down payment, and then purchase that vehicle. This way, you have a security deposit and the dealership is not at a total loss. Often time, the auctions allow guests, so take the customer to see that vehicle prior to purchase, or show him or her photos of it, so they can get a sense of what to expect.

3. Set up a time frame. If a vehicle does not sell within a certain amount of time, then try to sell it at a lower price, closer to what the dealership paid. Although it is not a big profit, we can always break even. Push the sales representatives to show that particular vehicle as an alternative option to the customer. Set "special prices" and promotions so that customers are aware that they are getting good deals.
4. As a last resort, sell the vehicles that do not sell for a long period of time to other dealerships. Most commonly, the dealerships will offer a low price, possibly even lower than what we paid for it. However, if the car did not sell for a half of a year, it is a possibility that the value of that vehicle depreciated anyway. Even though the dealership will have to sell it for a lower price, it is still not a total loss. By

getting rid of these vehicles, Sesame Street Auto Group will, in return, at least get most of the money back.

By implementing some or all of these methods, there will be more opportunities for Sesame Street Auto Group to purchase other cars that are in high demand. It will allow our lot to have to space, so that we can fill it with cars we know will make us a bigger profit. Also, it allows for the inventory to be constantly rotating, so that we do not have cars sitting at the dealership for several months at a time.

CONCLUSIONS AND RECOMMENDATIONS

Sesame Street Auto Group spent \$290,250.00 last year on vehicles that the dealership has not yet sold. Even though our company is profitable, profits could be higher.

There is a clear distinction of what costumers wants and what we provide. Vehicles that are in high demands sell more quickly and more often than those not.

The solutions are simple, and by implementing these methods, we can ensure that the dealership will not lose as much money and potentially make a profit.

1. Sesame Street Auto Group has to refrain from buying vehicles that are obviously not selling. By us not selling cars, we do not make any money, and, in theory, a we lose money.
2. Take requests from customers. If they are really interested in a particular vehicles, search for that vehicle. Once you find it, have them put down a security deposit or their down payment.
3. If it takes more than a few months for a vehicle to sell, this is a sign that we have to do something to promote it. Set up a special price or have sales representatives offer the customers to look at it as alternative options. Even if we decrease the price, it still makes us some profit.
4. If the car clearly does not sell on our lot, perhaps some other dealerships will have better luck. Sell the vehicles that are not selling to other car dealerships for a low price. This is a last resort, only because the other dealerships will try to make a low ball offer. This is not unrealistic, considering the fact that the value of cars decreases on a monthly basis.

The money that the dealership will earn can go towards other expenses, such as increasing the salaries of loyal employees or the office renovation we had planned for the past several months. The bottom line is that by taking the correct approaches, the dealership will maximize its profits to their full potential.