

The Full Spectrum Solution to Lost Sales

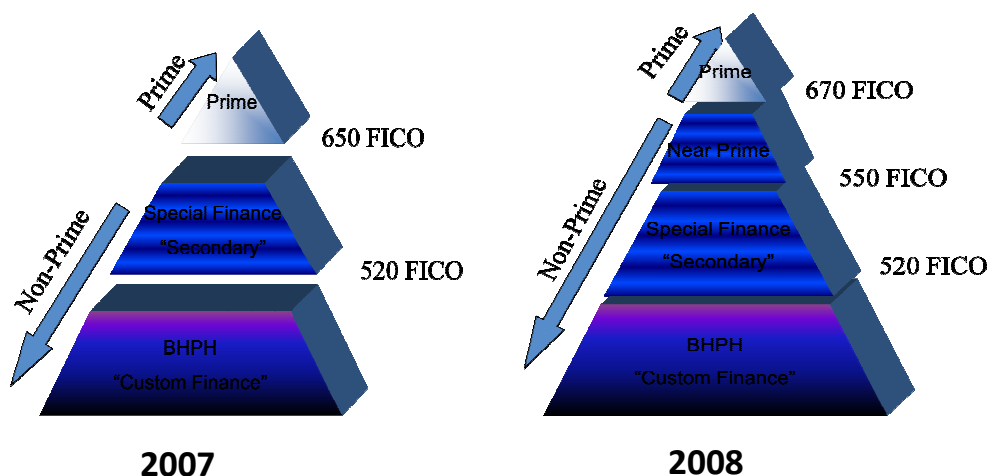
By Tom Herald

There has been tremendous change throughout the auto industry over the last year to say the least, and from all indications, it doesn't look like the dust is going to settle any time soon. The best way for me to describe automotive financing today and in particular, *Special Financing*, is to compare it to 1980 when the choices for consumers with credit problems were much more limited than they were the first half of 2008. There were local banks, a few specialized lenders, and buy here pay here. That was pretty much all we had. Now in reality it may not be that bad but it sure feels like it. Since the summer of 2008, we have lost more than 40% of our ability to finance automotive consumers.

Dealerships throughout the country are struggling to finance customers with a credit score below 550 today, the fastest growing segment of the industry. It is very difficult to find deals in this "no man's land" of lending and when the dealer finally gets one, the customer has no money for a down payment. This is a common theme all across the country – dealers have plenty of customers with poor credit and no money down. And the bottom line result is no deal. More and more customers are leaving dealerships via public transportation than in newly purchased vehicles.

The solution to this magnanimous problem for dealers lies in one of the *Key Fundamentals of Special Finance – Full Spectrum Finance*. Full spectrum financing is an absolute necessity for car dealers today. It affords them the ability to offer vehicle purchasing options to every customer who visits the store, regardless of their credit and with less emphasis on down payment. It removes an important limiting factor from the typical sales process and if done correctly, will help dealerships build customers for life by making financing as simple, seamless, and as profitable as possible.

Full spectrum financing covers the full spectrum of consumer credit scenarios. Over the past six months we've had to add a new tier to our *Credit Pyramid* that depicts this spectrum– The No Man's land between a 550 and a 520 FICO score. We did so in order to better explain the market today (Refer to Figure 1). Most dealers have no problems financing customers with a 550 score or better. It's this third tier however that presents the most problems. It is the one that's growing the fastest due to the recent credit crisis, but it's also the one that lenders are shying away from. And, at the same time, it is one tier where customers aren't quite ready to accept a buy here pay here loan.



The prime tier is easy. It's not hard to find good lenders to finance prime customers. In the near prime tier you will still find competitive lenders who are large and progressive and may even buy down into the upper echelon of the third tier. Small regional banks and local credit unions are great options to have in your repertoire especially if you build strong, profitable relationships with them. You will find them to be strong business allies that are in it for the long haul.

Like I said earlier the third tier is a whole different story lately. This is a segment of the business where we really have to rethink our game plan and may even have to take an entirely different approach to sales and finance. HSBC is out. Triad is only servicing loans. Wells Fargo recently bought Wachovia and no longer offers indirect lending. Americredit has struggled for quite awhile securing capital and managing growth. And as a result, Capital One is tightening their belt since they have unintentionally doubled their market share. All in all, we have lost over 40% of our financing ability in the industry and the majority of that loss occurred in this third tier where the recent credit crisis has forced a large percentage of the population.

In order to be effectively finance customers in this new third tier of the credit pyramid, we have to take a closer look at the Four P's of business:

- People – A dealer's staff must be proficient at finance with a thorough working knowledge of every lender's program that operates in this tier. The staff must be adequately trained in a sales approach that effectively develops the customer's real need early and focuses the sale away from specific vehicles. Every member of the team must be held accountable for generating results. There is neither time nor room for a freelance sales approach, particularly with this tier of customer.
- Process – A strict adherence to a proven "Road to the Sale" can save even the weakest of teams. The sales and finance process are intertwined in special finance, particularly in this third tier, and your procedures should be second nature to every member of the team.
- Product – Your inventory will make or break your deals. The days of 84 month terms and 150% LTV loans are gone. That's why I strongly urge you to buy and maintain a 45 day supply of inventory for this tier with an ACV between \$5,000 to \$7,500 and at least a \$1,000 spread behind book, mileage between 50K and 75K, and an age of no more than five model years old. Anyone saying you can't find these vehicles is simply wrong. Call me and I will put you into contact with dealers in several States who can help you. Remember to purchase your inventory by considering your financing options on the lot. I recommend that you factor a \$1,200 down payment, 48 – 60 month terms, your State usury rate for interest, and a lean, "safety only" reconditioning policy. This will help ensure that you maintain an adequate supply of inventory for the credit tier of highest demand.
- Promotion – You don't have to spend a lot of money advertising for customers in this tier. If you're like most other dealerships, you already have plenty of customers who fall into this category of financing and my primary focus would be to concentrate on these existing customers first. You can waste a lot of time and money trying to force a market that is not ready to buy. My advice is to purchase and manage good sales leads until you can develop the ability to generate them on your own and, demand in the first and second tiers returns.

The fourth tier, custom finance, is where most dealers fall short. Even dealers who have been involved in special finance for several years tend to ignore this category of financing either out of fear, or from a lack of understanding. Whatever the reasons, they just don't seem to have the stomach for the buy here pay here class of customer. To me any dealer who is not actively engaged with their own Related Finance Company (RFC) or BHPH operation is missing an incredible opportunity for sales and profits that can be an integral part of their business.

There are several very strong lending sources who are experts at this level of financing and collections if you choose not to tote the note yourself. Credit Acceptance Corporation, Westlake Financial, Western Funding Inc (WFI), Drive Financial, and sub-prime auto leasing companies like Auto Trakk are all great business partners that are thriving right

now and can help you sell more customers by expanding your spectrum of financing. They will give you the ability to finance buyers in both the third and fourth tiers of the credit spectrum.

Dealing with change is not optional. We have to be tactically minded and proactive in our thinking; we must meet the needs of the consumer by understanding the market and offering solutions that work. Full Spectrum financing allows a dealership the ability to sell more cars to more people, and evolve with the demands of the market.

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