White paper

Data tools evolve to give dealers an edge in a tight sales market

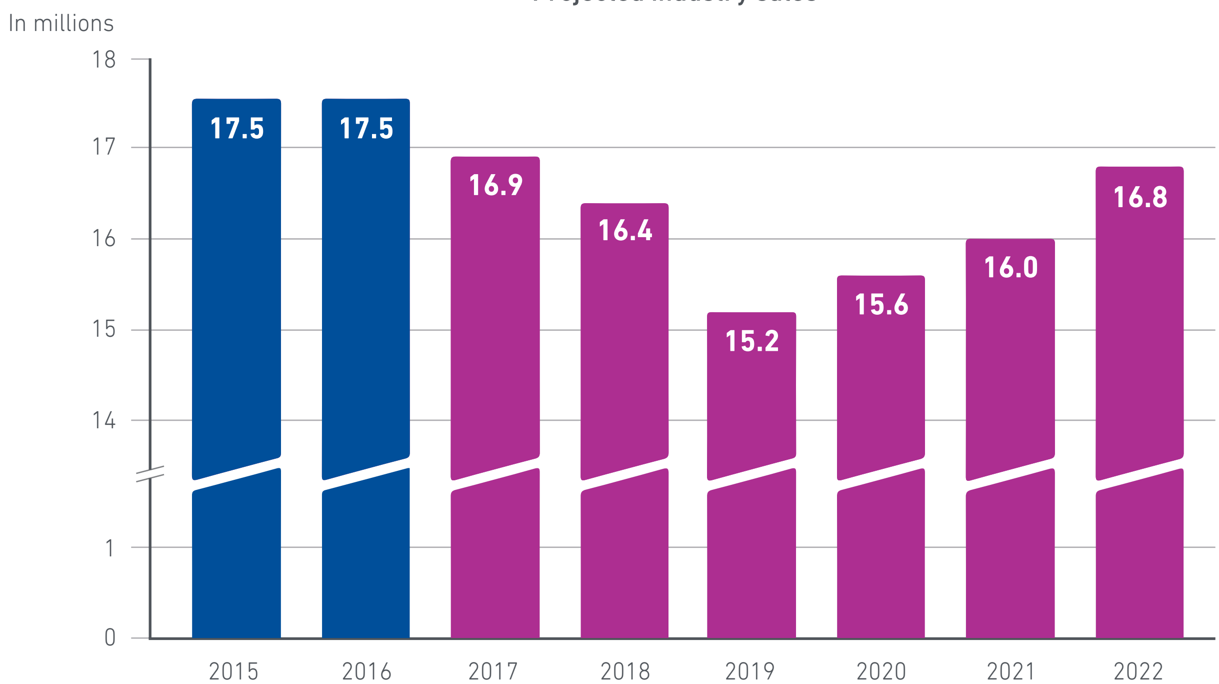
The automotive sector is the second-largest industry in the United States, generating $953 billion in annual economic activity and supporting 7.25 million jobs, according to the Alliance of Automobile Manufacturers, an industry consortium that tracks automotive trends. In 2016, there were more than 265 million vehicles in operation (VIO), nearly 17.5 million new vehicle sales (13.1 million retail and 4.4 million wholesale), nearly 40 million used retail sales, $1 trillion in loan balances and more than $75 billion in marketing spend ($35.5 billion in advertising and $40 billion in incentives).

Over the past seven years, the industry has shown great resiliency, bouncing back from a low of 10.4 million new vehicle sales in 2009 to nearly 17.5 million new vehicle sales last year.

> "U.S. auto sales last reached 'high tide' in 2000 and remained there through 2007."

During this period, manufacturers and their retailers have ridden a wave of industry growth to record impressive year-over-year sales gains. But that growth appears to have reached a "high tide." After reaching a high of 17.5 million last year, new vehicle sales have dipped in 2017, with a projected sales rate of 17.1 million, according to AlixPartners. The company predicts that sales will remain between 16.9 million and 16.8 million from now until 2024.

Projected industry sales

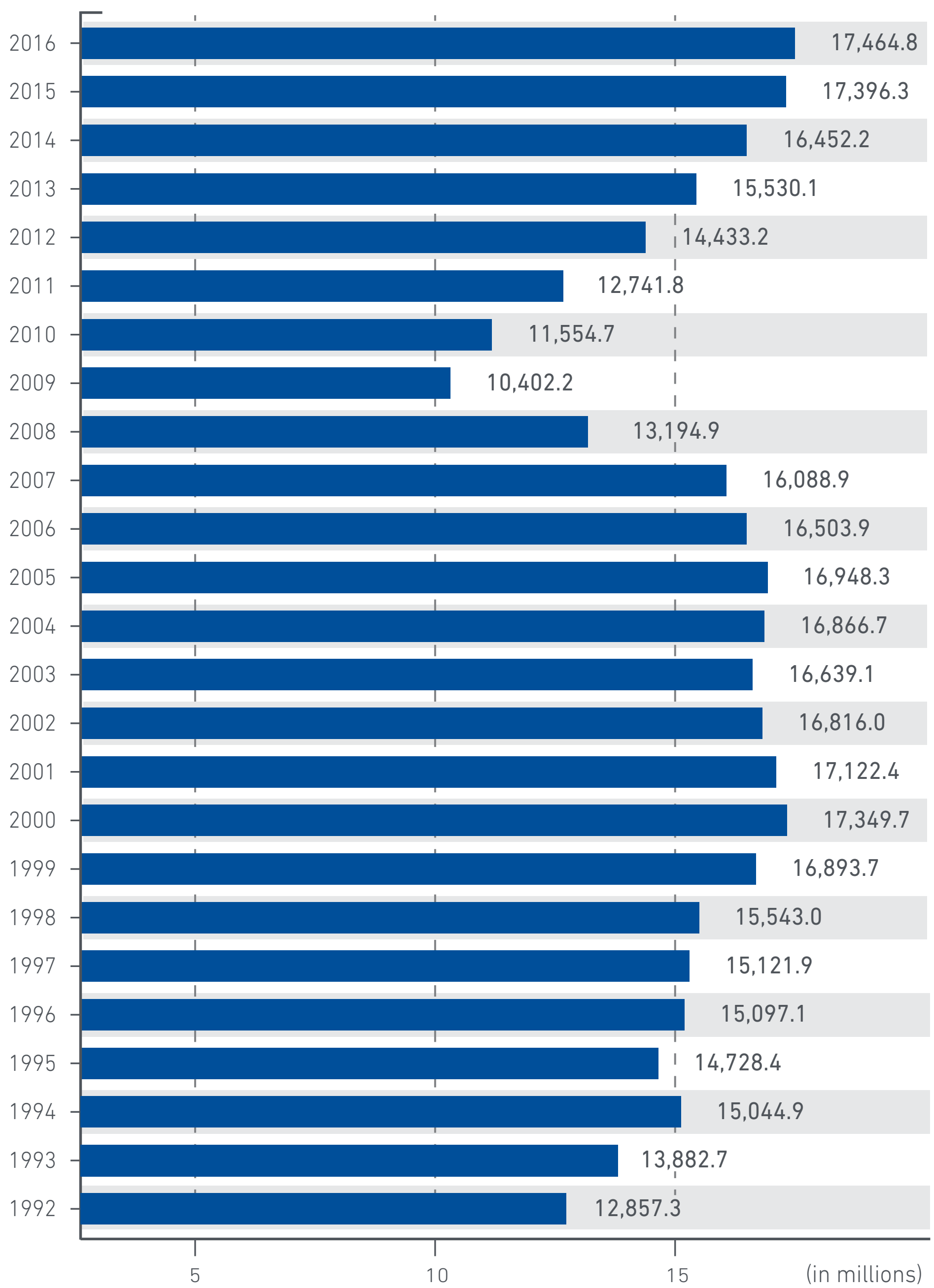


Note: Main drivers are used vehicle prices, GDP <3%, credit tightening/rates increasing and OEMs maintaining discipline.

Source: AlixPartners US auto forecast & analysis 2017 version (2019 trough remains unchanged from prior forecast in 2015)

U.S. auto sales last reached "high tide" in 2000 and remained there through 2007. During this time, automotive manufacturers chose to maintain production at the same levels to "keep the plants running" and thus created supply where there wasn't true demand. Ultimately, manufacturers increased incentive spending to "move the metal." Of course, this helped erode profits.

U.S. light-duty new vehicle registrations



Source: Experian

The industry is in danger of repeating history in 2017, as inventories have already begun to creep up. For example, as of Sept. 1, 2017, Ford had 111 days worth of unsold Mustangs, an 87-day supply of Fusions and a 103-day supply of Transit vans, according to *Automotive News*. Automakers aim for 65 to 70 days of inventory of most models.

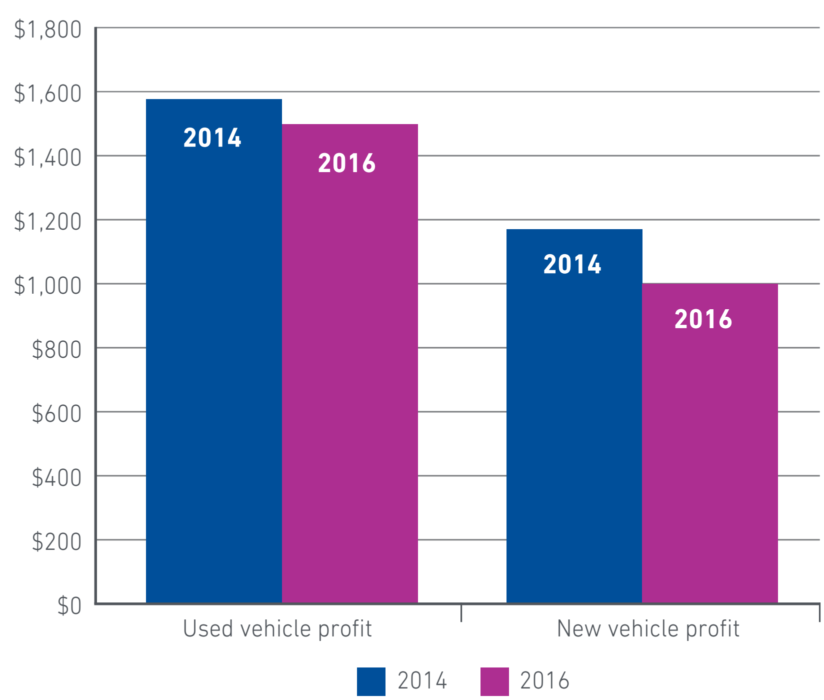
The industry is already reacting predictably to the inventory glut by incentivizing sales to move vehicles off dealer lots. Average manufacturer incentive spending per unit in August 2017 reached a record for the month at $3,805 per vehicle, surpassing the previous high of $3,645 per vehicle set in August 2016.

Further exacerbating the vehicle inventory situation are the nearly 3 million vehicles coming off lease in 2017. This creates price pressure in two separate directions. First, many customers opt for a low-mileage used vehicle instead of a new vehicle. This negatively impacts demand for new vehicles. In addition, the glut of low-mileage used vehicles puts downward pricing pressure on higher-mileage used vehicles.

Both of these scenarios will likely further erode profits at the retail level, and profits for both new and used vehicles already dropped from 2014 to 2016.

According to NADA, the average dealer gross profit on a new vehicle sale in 2014 was $1,152. In 2016, new vehicle gross profit dropped to $999 per vehicle. Gross profit on used vehicles was relatively flat over the same time period. In 2014, used vehicle gross profits were $1,565, compared with $1,515 in 2016.

Gross profit per vehicle sold is shrinking



Source: NADA

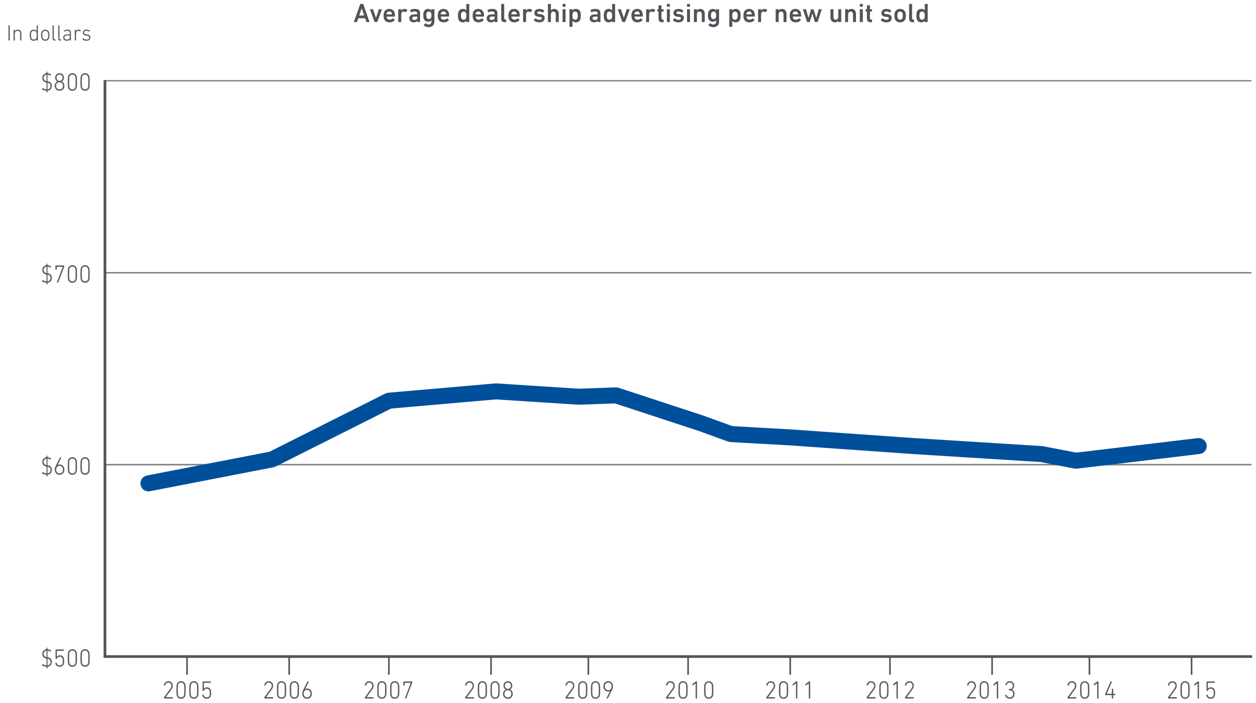
Part of the reason for slimmer profit margins is an increase in dealer advertising on a per-vehicle basis. Advertising cost per vehicle jumped from $607 in December, 2015 to $628 in December, 2016, a 3.5 percent increase. That's nearly three times the rate of inflation, which was 1.26 percent in 2016, according to InflationData.com.

Overall, the average automotive retailer spends approximately $525,000 annually on advertising and marketing. Dealers must find new methods of spending their marketing dollars to help move vehicles off the lot at a lower per-unit price.

There is no question the industry is facing pressure from several different angles. Manufacturer incentive spending, higher advertising costs, a glut of new and used vehicles and low to flat future sales projections are taking big chunks out of dealer profitability.

The key question:
What technology investments can dealers make and what marketing tactics can dealers deploy today to protect and grow their market share in a flat market?

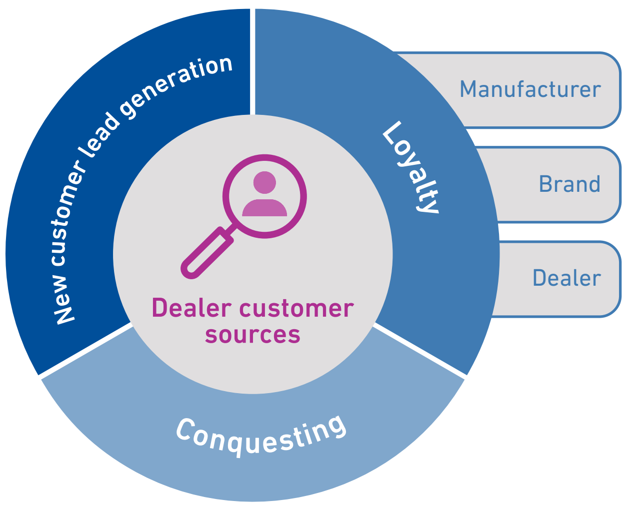
Average dealership advertising per new unit sold



Source: NADA

Where do dealers find customers?

It's important to define how dealers attract customers. For the sake of simplicity, customer acquisition can be broken into three primary buckets: new customer lead generation, loyalty and conquesting.



New customer lead generation — the practice of getting new customers in the door who have no prior automotive retail relationships.

This could be a first-time new vehicle or used vehicle customer, a customer who is new to the market, or perhaps a customer who has previously bought private-party used vehicles and is now looking to purchase from a dealer.

Loyalty — the practice of bringing back repeat customers. Loyalty, of course, has different definitions:

- **Manufacturer loyalty** is when a customer owning a brand of vehicle within a given manufacturer's portfolio of brands returns to market and purchases any of the brands of that manufacturer. For example, a Chevrolet owner returning to market and purchasing a Cadillac would be considered loyal to General Motors.
- **Brand loyalty** is defined as repurchasing the same specific brand of vehicle. For example, a Chevrolet owner would come back and purchase another Chevrolet.
- **Dealer loyalty** is defined as a customer from a particular dealership going back to that dealership to make another purchase.

From the automotive retailer perspective, the only loyalty that truly matters is dealer loyalty. A customer could remain manufacturer or brand loyal and still end up at a dealership across town. And even when customers are dealer-loyal, it can only take a dealer so far. Typical loyalty rates hover around 50 percent. If a dealership were to retain only 50 percent of its customers and not attract any others, they'd be out of business pretty quickly.

Conquesting — There are two definitions for conquesting. Dealers often refer to any new customer acquisition as a conquest, and this is often accomplished through traditional mass-marketing techniques.

A second term, advanced conquesting, involves using sophisticated data analysis to define and precisely target marketing efforts to competitors' customers — with the end goal of winning them over as your own.

It's important to note that this doesn't mean luring customers from another dealership of the same brand. If you're a Ford dealer, conquests should come from outside the brand and manufacturer.

In a flat market, conquesting is more important than ever. With fewer customers coming through the door and loyalty rates hovering around 50 percent, dealers who excel at advanced conquesting will be the most successful in current market conditions.

Mass-market approach inefficient, ineffective

To understand the importance of the analytic marketing tools available for advanced conquesting, it helps to review why mass-marketing effectiveness has diminished. In tight sales markets, dealers often revert to their comfort zone — traditional advertising. This often means returning to a shotgun approach to marketing and media efforts in the hope that blanketing the entire market with traditional television, radio and print advertising will get more people in the door.

But today's fractured media environment doesn't drive showroom traffic cost-effectively. In the not too distant past, the typical local market had a daily newspaper, three or four television stations and a handful of radio stations. Dealers made their ad buys, and customers magically showed up in lots.

Today, the local newspaper is still in print, but people have increasingly migrated to the online edition. Fans record their favorite television shows and fast-forward through the commercials. Mobile phones proliferate, and social media sites garner significant customer mindshare. Even if a traditional ad reaches a prospect, how do you know that prospect is in the market?

Automotive retailers need a much more sophisticated approach to ensure their marketing spend is both efficient and effective. This requires understanding the different data sets available and using them to create highly targeted marketing campaigns.

Deeper understanding of local market, competition key to conquesting success

It's relatively easy for an automotive retailer to focus on loyalty programs. After all, the data needed to implement a successful customer loyalty program resides in their own DMS, CRM system and daily interactions with customers.

Conquesting, on the other hand, is a bit more challenging. Competitors control the information needed to target those prospects. And those competitors certainly are in no hurry to share their customer information.

Fortunately, many emerging data tools can help retailers better understand their local market — both the demographics of the market's customers and the market's unique vehicle sales trends. When combined with other data points such as psychographic information, credit data and vehicle equity, automotive retailers can break a mass audience into smaller, more alike customer groups with a higher propensity to buy.

Advanced conquesting relies on several layers of market data:

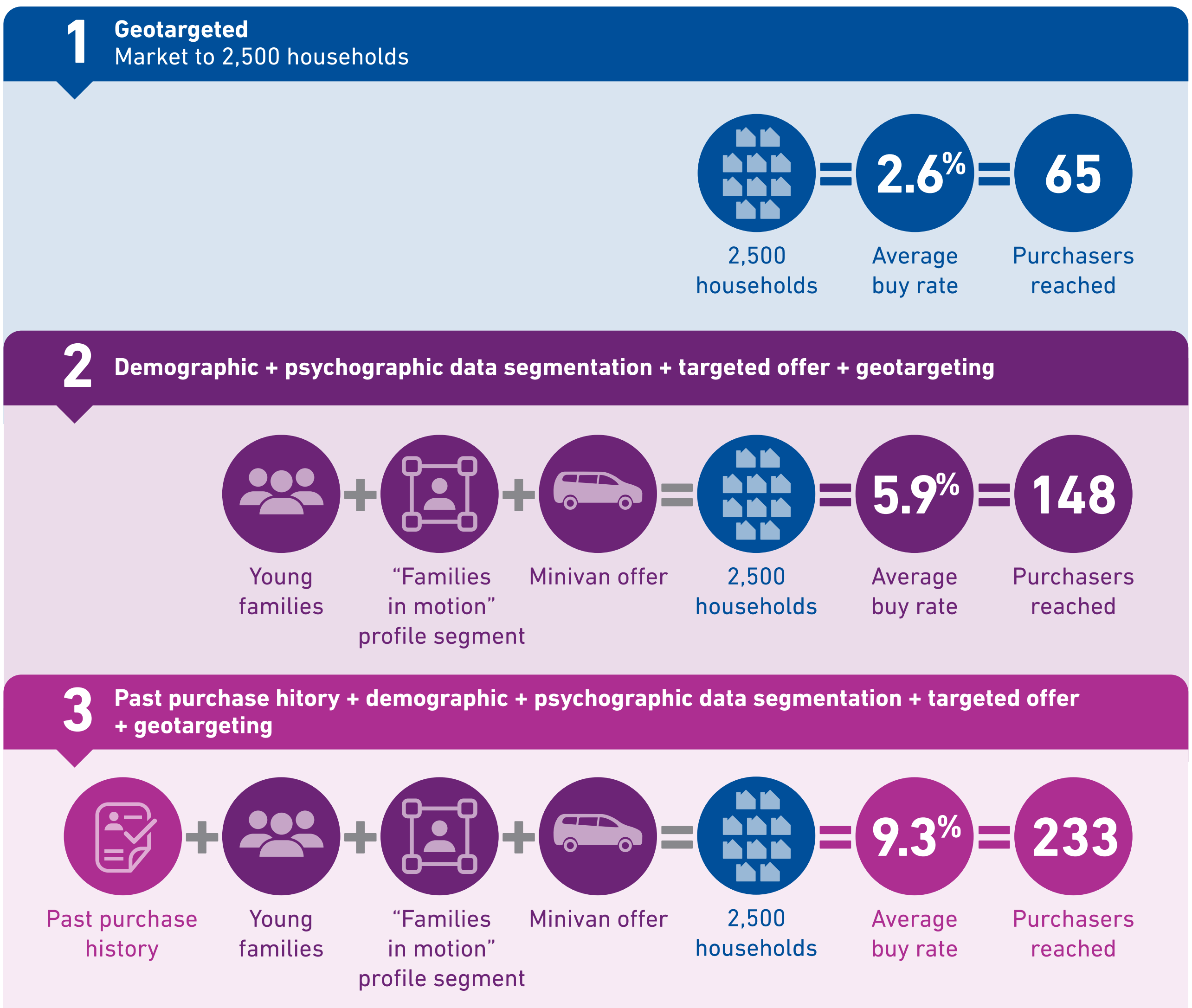
- **Understanding the demographics of your market —** Every retail market area has its own unique demographic characteristics. Does it skew older or younger? Are there more married couples with families than single people? Does it have a higher level of subprime customers? Are there more college-educated people there? Knowing these data points, figuring out how your manufacturer's product mix meets their unique needs and building marketing programs around these traits will help boost closing rates.
- **Understanding the demographics of key competitors' customers —** Sometimes a particular competitor can attract a certain niche customer. Perhaps they are the Corvette King and attract single males, or they have a preponderance of families purchasing SUVs and minivans. Knowing the unique customer attributes of key competitors can help dealers build marketing programs that target those customer groups and help woo them away.
- **Knowing what products are currently hot in your market —** Vehicle sales trends can fluctuate from market to market and do not necessarily emulate national trends. Perhaps a particular market has a higher concentration of families, and SUVs and minivans beat the national average. Or perhaps a particular market is far from a core city and more people are buying high-mileage vehicles for longer commutes. Knowing these trends can help with product planning and creating specific marketing initiatives to focus on hot-selling models.
- **Knowing your own hot-selling products —** What vehicles have been flying off your lots, and are these vehicles similar to vehicles sold by competitors? If so, building marketing initiatives targeting owners of similar vehicles to a dealer's hottest models can yield significant results.
- **Knowing which competitors' customers are coming off lease —** Customers with vehicles coming off lease are highly likely to make a new purchase or lease. It's easy for a dealer to track their own lease customers and build loyalty programs to get customers back in the showroom. But detailed insights into the competitive lease portfolio can create a pool of immediate conquest targets.
- **Understanding media habits of various consumer groups —** It's not enough to have the right vehicle for the right audience. In today's proliferated media market, it's critical to understand customer media habits. What customers respond best to direct mail? Online ads? What television shows are they more likely to watch? Unlocking the right media channels is the key to driving showroom traffic with qualified, interested potential buyers.

How are some of these concepts put into practice? Think about a metropolitan area with 100,000 households. If a marketer engages in a mass-market ad campaign, it means firing out ads to every household with no thought to who is currently in-market to buy. Simply blanketing a mass audience like this yields a 2.8 percent average buy rate.

Segmenting that audience with demographic and psychographic data will help identify a smaller group of households to create a smaller but much more targeted audience.

For example, an automotive brand campaign which is geo-targeted to 2,500 households will reach an average of 2.6 percent of consumers who are currently in-market and will actually purchase a vehicle. Targeting the same number of households by adding demographic and psychographic profiles, paired with an offer on an appropriate make/model, can increase the effectiveness to a 5.9 percent buy rate. Taking it another step, what if you also target by using past purchase history? Now you've zeroed in on the 2,500 households that can yield an average 9.3 percent buy rate.

The Evolution of Data Driven Conquesting Campaigns



What are some tactics that can be employed?

Using and analyzing data can help dealers make informed decisions rather than relying on their gut instincts. If you're a Honda dealer, conventional wisdom says conquest Toyota – they consistently show up in the list of cross-shopped makes for Honda, regardless of the market. But Toyota buyers are highly loyal. A more effective strategy? Go after Kia or Hyundai customers who are more likely to defect instead.

Dealers should focus on bread-and-butter models. They might be amped up to have a new shipment of electric vehicles or a high-end sports car, but those "specialty" buyers are going to find you. For the highest conquesting impact, focus on volume. For example, a BMW dealer should focus on the 3 Series against the Lexus 350 ES.

Dealers should choose three to four ZIP™ codes in their PMA where demand is highest. It may be tempting to try to lure away buyers further afield, but you're likely to lose on the front end and back end on every sale that's more than 20 miles from your dealership. Remember, you're looking for buyers who are easy to lure and have a good shot at becoming loyal service customers.

One key to succeeding at conquesting is to use digital tools for more precise customer targeting. Leveraging data and analytics is a much more efficient method for identifying groups of in-market customers.

Keys to succeeding at conquesting

Credit-based marketing
This approach combines all the demographic and psychographic information above with purchase history and credit data.

Equity-based marketing
If a customer has positive equity on their current vehicle, they are much more likely to make a new purchase. Again, when combined with demographic and psychographic data, equity-based marketing can significantly improve success rates.

Omnichannel marketing
Reach consumers with consistent messaging across multiple media channels, including online, social, traditional media and direct mail.

Automotive advertising response analysis
This provides the ability to measure campaigns for effectiveness and make adjustments to improve the overall response.

Advanced advertising solutions
Use advanced targeting in cable television to place an ad for a specific product in a particular household. For example, one household might get an ad for an F-150, but their neighbor might get an ad for a Mustang.

Market more competitively than ever; data tools can make the difference

In the competitive, tight market faced by dealers today, automotive retailers need to battle for every sale they can get. Mass-market techniques that worked as recently as a decade ago are no longer the most efficient method for driving sales. To effectively understand the market and win customers from competitors, dealers need analytic tools that can break a mass audience into well-understood segments of customers who are ready to buy.

Fortunately, technological advances have made these tools available to small and midsize dealers. They are relatively easy to implement and require a manageable investment. These tools also can be tracked to show a precise ROI, making them as popular with the dealership owner and CFO as they are with the sales team.

Going forward

To learn more about how data tools are evolving for dealers to provide them with an edge in a tight sales market, contact your local Experian sales representative or call 1 888 853 3307.

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