



Where Is the Financing Coming From?

Today's financing terms remain more limited than they were before the recession. For the most part, the limited number of recent loans has had higher spreads over the London Interbank Offered Rate (LIBOR), lower loan-to-values, and shorter repayment terms. However, some large banks are looking to expand relationships with existing clients and pick up new clients. Given a well-capitalized buyer and a solidly profitable store, certain banks might, in limited circumstances, offer 70 percent loan-to-value on real estate and up to 50 percent blue-sky financing, in addition to floorplan financing.

A few of the captive finance companies are also active in assisting buyers. A recent buyer for a luxury store accepted a loan package that had 80 percent loan-to-value real estate financing and a loan for 50 percent of the blue-sky and 50 percent for working capital requirements. This loan required collateral and personal guarantees.

Why Are Owners Selling Now?

Almost all dealerships are making less money now than they did during the boom period from 2002 to 2006. Few people believe that new car sales will reach that level again for many years. Retail dealerships spent 2009 reducing their expenses, and, as a result, many are seeing upticks in profits and margins. These upward trends have the potential to increase the sale prices for these dealerships. For some dealers in their 70s or 80s, however, it is simply not worth waiting for an economic recovery before beginning a sale process. With the worst of the depression in auto retail behind them, these dealers want to begin enjoying their retirement now.

Thinking Beyond Today

Buyers are thinking long term, offering improved multiples over recession lows on trailing earnings for desirable franchises as well as offering blue-sky for franchises that are highly desirable even if they are not currently profitable. Because these buyers believe the next five to 10 years will be highly profitable for them, they are willing to make aggressive offers to buy the right stores in the right markets. Sellers know that future profits likely will be higher than current profits. To get an owner to accept an offer now, buyers are enhancing their offers to close the pricing gap, which results in sellers sharing in some of the future upside of a dealership at the time of closing. While many in the auto industry thought that blue-sky net income multiples would fall from their previous high levels, this has not proved to be the rule when looking across the recent transactions for high-quality luxury and midline import dealerships. Absolute valuations are down from peak years, but multiples of trailing earnings are still strong for attractive franchises.

Tax Implications

Potential tax changes might also be driving dealers to consider selling now. Many experts believe that President Barack Obama's administration will not renew the Bush tax cuts, potentially resulting in as much as a 67 percent increase in the federal capital gains tax rate should the rate increase from 15 percent to 25 percent. Dealers might not see the point of working to increase earnings over the next couple of years before selling their stores if some, or all, of the incremental purchase price is going to be paid to the government.

Blue Skies Ahead

The market for buying and selling auto dealerships has begun to thaw and is stronger than many dealers might expect. Well-capitalized buyers looking to put capital to work early in the economic recovery are getting attractive financing from OEM lenders and banks. Sellers of attractive franchises are seeing strong blue-sky multiples with some looking to sell before capital gains taxes increase.

Note: Under U.S. Treasury rules issued in 2005, we must inform you that any advice in this communication to you was not intended or written to be used, and cannot be used, to avoid any government penalties that may be imposed on a taxpayer.

*Rick Kotzen is a partner with **Crowe Horwath LLP** in the Fort Lauderdale, Fla., office. He can be reached at 954.489.7430 or richard.kotzen@crowehorwath.com*