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When Gordon Stewart sought to expand his dealership group, he chose a Chevrolet store. He says a Toyota dealership would have been too expensive.

Small dealers can't afford price tags of best stores

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Sky-high prices for the most coveted auto dealerships in the hottest markets are shutting out traditional entrepreneurs.

These days, only public dealership groups and the largest private megadealers can afford to buy top-tier stores, dealers and analysts say.

By consensus, the most coveted automotive franchises are Toyota, Honda, BMW, Mercedes-Benz and Lexus.

Sheldon Sandler, founder of the Bel Air Partners investment firm, says those brands' dealerships easily command prices of $35 million to $50 million "for one good store -- not a great store."

As a consequence, Sandler told *Automotive News*, dealerships for the top-tier brands now take longer to sell. Dealers who would have bid for such stores five years ago are paying cheaper prices for lower-tier brands instead.

Gordon Stewart's Toyota dealership in suburban Birmingham, Ala., makes lots of money. But when Stewart sought to expand his private group of five dealerships, he chose to add a Chevrolet dealership in Georgia to his three Chevrolet franchises.

Stewart's group, based in suburban Detroit, isn't small. It ranks No. 112 on this year's *Automotive News* list of the top 125 U. S. dealership groups, with reported revenue of $253.7 million in 2006. But even with those resources, Stewart says the cost of another Toyota dealership would be too steep.

A Toyota dealership's "blue sky" -- the value of the franchise but not including "hard" assets such as real estate, buildings or inventory -- routinely exceeds six times its net annual pretax earnings, Stewart says. A successful Chevrolet dealership's blue sky typically is three times net earnings.

"I can have a return in three years instead of six or more," says Stewart, who also has a Hyundai franchise and brokers other dealerships.

Hit parade

Dealership broker Sheldon Sandler says these are the top-tier franchises.

- **Toyota**
- **Honda**
- **BMW**
- **Mercedes-Benz**
- **Lexus**

Higher bar

The growth of public groups over the past decade has "raised the bar" on dealership sales, says John Pico, a Dallas consultant who advises dealers on acquisitions. Six of the seven largest U.S. dealership groups are publicly traded.

Brady Schmidt, president of National Business Brokers in Irvine, Calif., says prices of top-tier import- and luxury-brand dealerships have escalated sharply in the past two years.

As public and private consolidators prune unwanted franchises from their dealership networks, Schmidt says, demand for the top brands is more intense. Toyota and other leading import brands are gaining U.S. market share. And their dealership networks are much smaller than the Detroit 3's, Schmidt notes.

"It's the law of supply and demand," says Schmidt, whose company works with more than 2,000 dealerships.

Some dealers who cashed in by selling to public groups are paying big bucks to get back in the business now that their noncompete agreements have expired, Schmidt says. And successful automakers such as Toyota and Lexus are demanding new or renovated stores, he adds.

"The average buyer who wanted to buy a Toyota store five years ago does not now want to spend that kind of money -- or he can't afford it," Schmidt says.

Rather than adding large numbers of dealers, Toyota Division is asking current dealers to expand, says a northern California dealer who asked not to be identified.

Instead of opening a small dealership in a city of 150,000 residents, the dealer says, Toyota wants a dealership in a nearby city of 300,000 to absorb that market area. That plan could cost $40 million to acquire land to expand the dealership site and $16 million for a new building.

Bob Carter, general manager of Toyota Division, concedes that the high cost of the brand's dealerships "makes it much more difficult to get started." But he calls the rapidly rising prices paid for Toyota stores "an indicator of confidence in the future."

Bargain hunting

Sandler, whose Skillman, N.J., brokerage works with dealers, says "a top-tier store in a decent market" will earn about $3 million a year. At six to nine times net pretax earnings, the dealership's franchise would have blue sky worth $18 million to $27 million, he says.

Costs of real estate and remodeling could elevate the dealership's sales price to $50 million or more. "Few individuals want to make that kind of commitment," Sandler says.

A top-brand dealership that once might have sold in a year now stays on the market for two to four years, he says. Traditional entrepreneurs who want to buy dealerships are concentrating on less expensive brands such as Chevrolet, Nissan and Cadillac.

Says Sandler: "They don't have to worry about competition from public companies."

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