BusinessWeek

It's Official: Chrysler to Close 789 Dealers

Posted by: David Kiley on May 14

Nearly 800 Chrysler dealers across the country got pink-slips today, unceremoniously delivered by United Parcel Service. In almost every state in the union, cities, small towns and remote hamlets, the auto company told 789 dealers, a number of whom have had dealerships in their families for generations, that they are out of the Chrysler business.

Usually, it is very difficult to terminate a dealer franchise agreement. But because Chrysler is operating in Chapter 11 bankruptcy proceedings, it is much easier—legally if not emotionally.

The cut adds up to 25% of Chrysler's dealer network. Four million customers who have bought and serviced their cars at those dealerships are affected and are being contacted by mail.

The number of dealers Chrysler is cutting is more than Saturn or Lexus has in total. The automaker, which is in process of merging with Italian automaker Fiat, had a high of about 6,500 dealers in the mid 1960s. Before this cut, it had 3181.

Chrysler is trimming its dealer network to lower its own distribution costs, as well as make the remaining dealers more profitable. Perusing the list of dealers, a large number sell only Dodge Trucks, or have Jeep-only franchises that have been acquired and stuck on to showrooms that carry brands that compete against Chrysler on the whole.

Indeed, many dealers, especially in rural areas, have out-of-date facilities and a hodgepodge of brands, such as a Jeep showroom stuck in with Ford-Lincoln-Mercury, or GMC-Buick-Pontiac. Steven Landry, Chrysler's executive vice president of sales, said that 345 of the targeted dealers, or 44 percent, are paired with a "competitive franchise that's stronger than ours."

Other cuts have been made in economically beleaguered areas like Las Vegas, Detroit, and Ft. Lauderdale, sapped by falling house prices and foreclosures. Dealerships being cut in Troy and Birmingham, Michigan, barely 15-minute drives from Chrysler's headquarters in Auburn Hills, MI.

The reason for culling the dealer list is obvious—there's a lot of inefficiency in the current system. Chrysler has said that 25 percent of its U.S. dealers account for half of the company's sales.

AutoNation, the world's largest auto retailer, is shutting seven Chrysler dealerships. Commenting on the consolidation plan, Mike Jackson, Chairman and Chief Executive Officer, said, "We believe Chrysler's consolidation plan is a difficult but positive step forward for Chrysler and the automotive retail industry. Dealer consolidation is a

necessary measure in today's automotive industry and will strengthen America's dealer network and improve dealer profitability over the long term."

A total of 658 of the rejected dealers, or 83 percent, already sell more used vehicles than new. But a dealer that loses its new-car business can get starved of new customers, as well as energy in the community. "You don't make as much profit on new cars as you do on used or in the service department, but it's kind of the blood flow through an operation," says Earl Hesterberg, CEO of Group 1 Automotive, a company that owns numerous dealerships including some that sell Chryslers.

Local communities who are losing dealerships will clearly see a rise in unemployment. Sales tax is often cited as another area of loss, but this is actually not an overall risk. "Dealerships may be going away, but customers are not. In other words, when a dealership closes, its customer may buy a competitive product, or buy from another Chrysler dealership. The sales tax is still being paid. The risk for communities is that the tax may shift to a different town," explained Edmunds.com CEO Jeremy Anwyl.

Another mistaken belief is that car companies will somehow save a significant amount of money by having fewer dealerships. In truth, there are only minor savings gained by cutting the regional staff required to serve a smaller dealer body.

The real motivation in cutting dealerships is to improve the profitability of the dealer. Stronger dealers can invest in better facilities and be generally more effective in their marketing. Indeed, Sageworks Inc. reports that profit per employee in privately owned dealerships has plummeted. As sales decreased so rapidly last year, profits decreased at an even faster rate. That's due to the high fixed-cost environment that dealers operate in. Dealership profits fell from $4,985.57 per employee in 2007 to a scant $133.02 per employee in 2008. As a result, unprofitable dealerships began closing over the last year on their own. But Chrysler's bankruptcy, and the possible bankruptcy of General Motors, is speeding that process.

GM is facing a May 30 deadline to square away a reorganization plan that will meet White House demands. If it cannot get bond holders to accept much less than they are owed, and union workers to accept big concessions, it also will reorganize under Chapter 11 and cut more than 2,000 dealers.