



Industry Commentary

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Auto Dealers Accelerate the Pace of Digital Transformation

Traditionally, buying a car has been one of the most high-friction, low-satisfaction transactions that most consumers encounter. But that is all changing. Spurred by the COVID-19 pandemic, auto dealers are racing to digitize their businesses and catch up with e-commerce retailing in the rest of the consumer world. Those that cannot embrace this transformation are likely to be left behind.

Transforming the Customer Life Cycle

Just two years ago, U.S. car dealers seemed relatively hesitant to transition to e-commerce. Dealerships continued to thrive on the traditional high-touch, brick-and-mortar model. But the COVID-19 pandemic caused dealers to quickly adapt as customers became more reluctant to shop in person.

Today, auto dealers are rushing to transform their businesses with digital tools designed to drive efficiency and increase customer satisfaction. This transformation is not confined to just the auto-buying experience. Digital transformation is taking place across the customer life cycle—from point of sale to financing and insurance to service and repair—as customers express their preference for ease, convenience, and fingertip optionality.

As digitization spread in 2020, buyer satisfaction increased meaningfully. According to a Cox Automotive survey, buyer satisfaction levels increased by 6-10% year-over-year across all key sales elements, including the buying process, trust in quoted price, interactions with the sales desk, and financing and insurance. Satisfaction levels were highest among “digital-heavy” customers.¹

In early 2021, 80% of dealers said they planned to offer more online options over the next two years, and 75% said they would not survive if they did not adopt digital retailing.² Annual global automotive software spending is projected to rise to above \$32 billion by 2026³, including sales and marketing, financing and insurance, dealer management systems, customer relationship management systems, and parts and inventory management.

Below, we look more closely at digital transformation in three key segments of the auto dealership: sales, service and repair, and financing and insurance.

New Sales Tools Drive Customer Satisfaction and Dealer Margins

The COVID-19 pandemic led to a decline in auto production as the industry dealt with a global chip shortage and other supply chain issues. Dealers also had to contend with depressed demand for new cars as consumers increasingly stayed home. Dealers held fewer vehicles on their lots and had to quickly switch their focus to online sales tools to allow consumers to broaden their search activity.

These new tools are transforming the

1. Cox Automotive, “Cox Automotive Car Buyer Journey Study, Pandemic Edition,” Media Summary, February 2021. “Digital-heavy buyers” are defined as those who complete 50% or more of their activities online.
2. Cox Automotive, “Digitization of End-to-End Retail,” Consumer Survey, January 2021.
3. Technavio, “Global Automotive Software Market 2022–2026.”

way people buy cars. Customers can look at different models and add-ons across manufacturers and compare prices online without having to visit multiple dealerships in person. They can interact with salespeople by chat and book a time to test-drive a specific car without having to look at the entire inventory on the lot.

In 2020, 38% of shoppers preferred to finalize their vehicle purchase price online, up from 25% in 2017.⁴ Buyers visited just two dealerships on average in 2021 versus 2.7 in 2016. Time spent at the dealership reached a record low of two hours and 35 minutes, while consumer satisfaction hit an all-time high.⁵

Surveys show that customers have been using more digital retailing tools since the start of the pandemic, and 76% of them are open to a fully online buying process.⁶ The traditional timeline of buying a vehicle has been shortened and streamlined as proactive dealers target in-market consumers and provide digital retailing tools to drive efficiency.

Digital Fix for Service and Repair

Service and Repair (S&R) is the number one profit center for the auto dealer. It is also a key area of opportunity to enhance the customer experience and boost retention.

Dealers have multiple opportunities to communicate digitally with customers around S&R, including service reminders, online cost estimates, progress check-ins, digital receipts, parts purchases, and vehicle inspection reports—a growing area of focus. Customers who have a positive experience in S&R are viewed as more likely to buy another car in the future from the same dealer or refer friends and family.

S&R, on average, generates more than 50% of dealership profits. Dealers make only about \$300 on the sale of a new car, but will make about \$4,000 on repair, warranty, and recall services over that same car's four-year warranty term.⁷

The rising age of vehicles on U.S. roads has boosted S&R revenues because older cars need more maintenance. This was exacerbated by supply chain issues that depressed production of new cars during the pandemic—only 3.3 million new cars were sold in the U.S. in 2021 compared to 7.5 million sold in 2015.⁸

Meanwhile, repair and maintenance costs are increasing. Similarly, the average price of repair per collision is expected to increase, which creates a substantial revenue opportunity for an industry which generates \$111 billion in services and part sales annually, an average of \$6.7 million per dealer.⁹

The growing market for electric vehicles is another factor. Analytical firm We Predict, now a part of J.D. Power, found that EV service-related costs for cars at the 12-month mark averaged 1.6 times higher than costs for comparable gas-powered vehicles. This is partly because EVs are newer and service shops take longer to diagnose and repair them—1.5 times the number of hours at labor rates that are 1.3 times higher than for gas-powered vehicles. However, this cost difference may narrow over time as the industry becomes more familiar with EVs.¹⁰

Cox Automotive expects dealers' S&R businesses to remain robust throughout 2022. The 2022 U.S. estimated number of motor vehicle registrations is 285 million, and we expect consumers to continue focusing on fixing rather than replacing vehicles as new vehicle prices remain high.¹¹

Focus on Financing and Insurance

Financing and Insurance (F&I) is another piece of the sales cycle where dealers have opportunities to increase both profit and customer loyalty.

Instead of viewing F&I as the final and tedious paperwork step in the sale process, dealers are increasingly addressing it early and leveraging new digital tools to improve the process.

Dealers have been somewhat wary of online F&I because it gives customers

more decision-making power over possibly complex financing and insurance decisions. Dealers that have moved online, however, report favorable outcomes helped by adaptations like simplifying the process and layering in human support by chat and video.

As a result, consumers are buying more coverage options. Insurance options are also expanding as customers display lower risk tolerances, perhaps partly due to the pandemic. Standards like vehicle service contracts are being augmented by policies for tire and wheel replacement, key replacement, and body protection.

We expect F&I to remain a key area of focus for auto dealers because F&I options lead the customer back to the dealers' service center and enhance brand loyalty. They also boost margins as transaction values rise due to car inventory shortages and as dealerships increase employee F&I training and product penetration. According to an Automotive News survey of the 150 largest auto dealership groups in the U.S., F&I revenue per vehicle increased for more than 60% of participating dealership groups in 2020. The top dealership group in terms of F&I revenue per vehicle generated \$3,558, an increase of 86% from 2019.¹²

The Future is Digital— But Not Entirely

Auto dealers were late in making the transition to e-commerce, but they are making up for lost time. The industry is in the midst of a wave of digital transformation across the entire customer life cycle.

Dealers are not merely responding to consumer demands—they are embracing the benefits of digitization from cost reduction to brand loyalty. Digitization offers more and cheaper options than the traditional model for ongoing communication with a customer. In a 2021 survey, for example, "digital-heavy" car buyers

4. Cox Automotive, "Digitization of End-to-End Retail," Consumer Survey, January 2021.

5. Cox Automotive, "Cox Automotive Car Buyer Journey Study, Pandemic Edition," Media Summary, February 2021.

6. Cox Automotive, "Digitization of End-to-End Retail," Consumer Survey, January 2021.

7. WardsAuto, "Going Digital to Improve Dealerships' Service Departments," March 10, 2021.

8. BEA, "Auto Sales – Seasonally Adjusted at Annual Rates (Millions)," June 2, 2022.

9. NADA, "2020 Annual Financial Profile of America's Franchise New-Car Dealerships."

10. We Predict, "The True Cost of Keeping Vehicles In Top Working Condition," May 18, 2021.

11. IBISWorld, "Number of Motor Vehicle Registrations," January 2022.

12. Automotive News, "F&I Profits Soar at Largest U.S. Dealership Groups," July 19, 2021.

consistently scored 10-15 points higher on dealer loyalty and trust than “digital-light” buyers.¹³

There is also a generational factor involved. For vehicle financing, 19% of Millennials and Gen Z signed a vehicle financing contract online vs. only 5% of Baby Boomers in the past twelve months.¹⁴ As the younger population’s share of vehicle registrations continues to increase, we expect digital transformation across the entire consumer vehicle life cycle to continue to expand.

Acceleration in the pace of digitization in the auto dealer channel has also meant a pick up in M&A activity.

Notable deals in the past 12 months include Cars.com’s acquisition of CreditIQ—an automotive fintech platform that allows customers to receive online loan approvals and buy F&I products from dealerships, and Asbury Automotive’s acquisition of Larry H. Miller Dealerships and its in-house F&I provider, Total Care Auto.

As auto dealers transform, we expect to see the continued emergence of

an omnichannel model designed to serve a spectrum of consumer preferences, from the brick-and-mortar traditionalist to the digital-forward customer who wants to do everything online without ever having to set foot in a dealership. Either way, the industry’s recent changes clearly show that auto dealers who do not fully embrace digitization will soon be left behind.

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13. Automotive, “Cox Automotive Car Buyer Journey Study, Pandemic Edition,” Media Summary, February 2021. “Digital-heavy buyers” are defined as those who complete 50% or more of their activities online. “Digital-light buyers” are defined as those who complete less than 20% of their activities online.

14. Cox Automotive, “Car Buyer Financing Journey,” April 2022.