

Automobile Dealership

RESEARCH REPORT

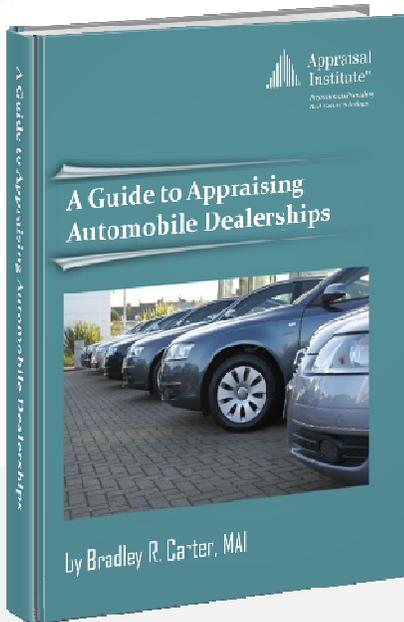
Greystone Valuation Services

Appraisal & Counseling

Year-End 2016



Winner of the George L. Schmutz Award



A Guide to Appraising Automobile Dealerships

by Bradley R. Carter

(ISBN: 978-1-935328-64-3)

The appraisal profession's first major work on the valuation of auto dealerships, this book offers defining direction on significant and controversial issues; published by the Appraisal Institute in 2015. **(Order here)**

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Recent and Upcoming Publications

The Valuation of Automobile Dealerships; Appraisal Institute Class (Upcoming - 2017)

Valuation Magazine (3rd Quarter 2015) – “Face Value” column (Interviews with the appraisal profession's thought leaders)

“A Guide to Appraising Automobile Dealerships” – Featured topic in *The Appraisal Journal*, (Summer, 2015)

How online sales are changing dealership real estate value, image programs, and more” – *Automotive Buy Sell Report* (July, 2015 Interview)

“The Rise of the Market for Auto Dealerships: Bad News for Landlords?”
- *Real Estate Issues*, (Volume 39, Number 3, 2014)

“Auto Site Selection” – September/October 2014 issue of *Commercial Investment Real Estate* magazine

Greystone Valuation Services, Inc., an Atlanta-based real estate appraisal and counseling firm, provides appraisal and counseling services related to 100+ automotive-related properties per year, including several of the largest and highest volume automobile dealerships in the nation.

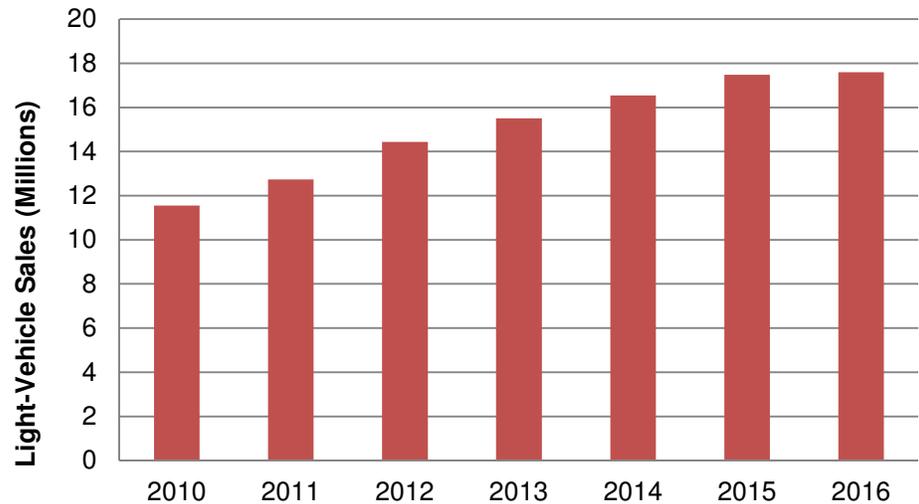
Recent engagements include appraisals of single dealerships or dealership portfolios in Alabama, Arkansas, California, Colorado, Connecticut, Florida, Georgia, Kansas, Illinois, Indiana, Louisiana, Massachusetts, Michigan, Minnesota, Mississippi, New Hampshire, Nevada, North Carolina, Ohio, Oregon, Pennsylvania, Rhode Island, South Carolina, Tennessee, Texas, Washington and Wisconsin.

Auto Sales and Profits

Demand for auto dealerships is ultimately a function of new unit sales, and the ability of buyers to purchase dealership properties is ultimately a function of profits.

- **Vehicle Sales Trends:** Sales have increased in each year since the recession and are now at a record level.
 - 2016 light-vehicle sales totaled 17.6 million units, a nominal gain from 2015.
“Pent up demand is effectively spent.”

**Total U.S. Light-Duty Vehicle Sales
2010-2016**



Source: WardsAuto, WWW.NADA.ORG

- **Post-Recession Sales:** From the 2010 through 2016, unit sales increased by about 50%, despite the decrease in the number of dealerships during that time. In 2016, though, **the market plateaued**; new units sold were 965 per “rooftop” and 548 per franchise (or brands sold at dealerships), essentially the same as in 2015.
 - **Near-Term Outlook:** Most analysts anticipate no significant near-term changes.
 - **Long-Term Outlook:** While forecasts vary, there are long-term threats to the current retail model that depends on large, expensive dealership properties.

“We are headed toward a stable market for U.S. auto sales, not a growing market”

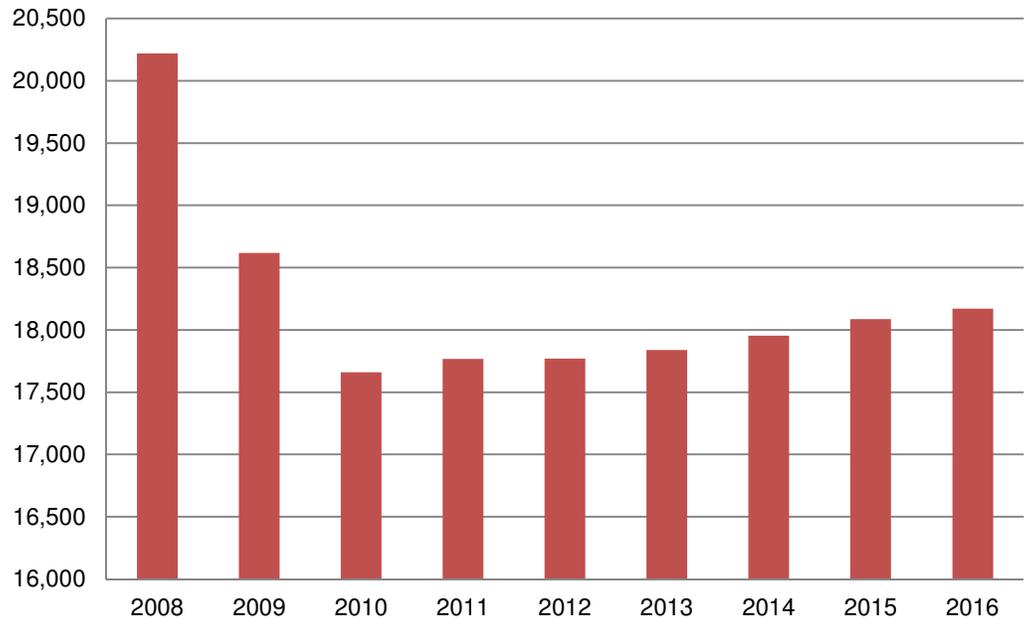
- **Auto Dealership Profitability:** Gains have been substantial since the recession, but with little recent growth.
 - Post-Recession Profitability - Average earnings per dealership achieved a **compounded annual gain of 23%** from 2008 through 2015.
 - Recent Profitability – While average earnings per dealership set a record in 2015, margins are dwindling. While complete information for 2016 is not yet available, there is anecdotal evidence that profit margins on new-vehicle sales continue to decline, and some dealers report **declining margins** for their entire operations.

Auto Dealership Real Estate Trends

National Inventory of Auto Dealerships

The last major change in the inventory of automobile dealerships is when it dropped by 8% from 2008-2009; since then the number of automobile dealerships has remained basically stagnant.

Number of Dealerships in U.S.



Source: Urban Science

Real Estate Trends

Factory Image Programs

Factory image programs continue to dominate the real estate component of automobile dealerships.

- Kerrigan Advisors' The Blue Sky Report echoes a sentiment we hear regularly:

"Most buyers are not looking for real estate development projects."

- Manufacturers want all their dealerships to have a similar look,

"Just like McDonalds."

- Dealers with strong balance sheets who receive a costly facility upgrade mandate from the OEM are quicker than ever to relocate from their old facility to a new, modern, compliant building that they construct themselves in the immediate area of their existing dealership. Therefore, **some of the strongest markets carry the greatest risk of having dealership properties go dark.**

Auto Dealership Real Estate Trends

Auto Dealership Pricing

Healthy pricing and increasing transaction activity resulted in **record volume for sales of auto dealership properties** in 2015 and then again in 2016.

How Prices are Established

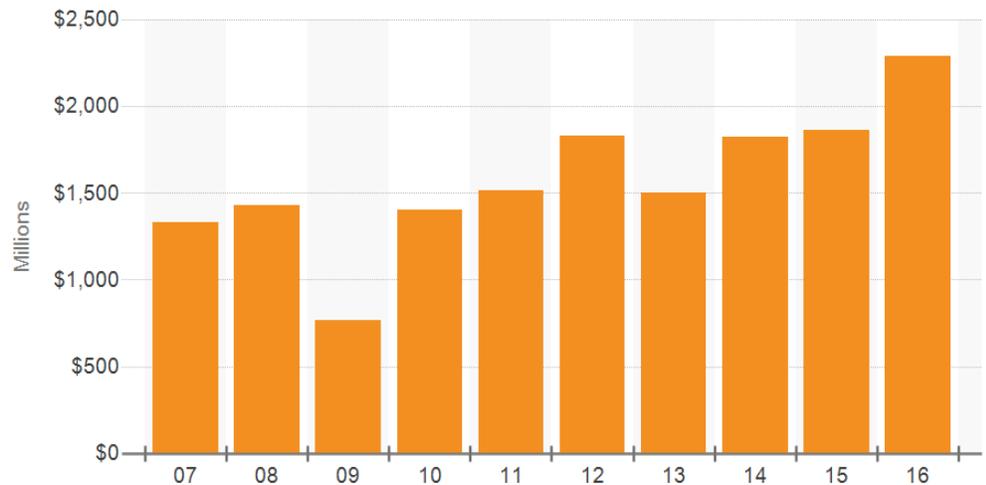
When operating dealerships are sold, it is usually a sale of the entire enterprise and what is reported as the “price” for the real estate is actually an allocation of the total price to the real property component. Greystone Valuation Services conducts an ongoing survey of auto dealership buyers and sellers regarding how these “allocations” (or the prices for the real estate that supports dealerships) are established. The most common responses are:

- Appraisal (by far)
- Depreciated cost
- “Whatever number minimizes the tax liability”
- “Whatever number maximizes the leverage of financing”

Other most common responses include:

- Book value
- Tax value
- Broker’s opinion
- Advice of the OEM
- “Whatever number keeps the OEM from getting involved”
- “Arbitrary”

Auto Dealership Sale Volume



Source: CoStar Group
Criteria: Auto dealership properties 10,000 SF+

Price Appreciation and Transaction Activity

It is clear that sales growth is slowing, perhaps even plateauing. According to McLarty Automotive Group founder Mark McLarty, as reported in Automotive News:

“The peak of it being a seller’s market is behind us.”

Some expect a mild contraction.

“Some of the ‘froth’ we saw” in late 2015 and early 2016 “has probably been blown away.”

Auto Dealership Industry and Market Experts

We regularly interview automobile dealership brokers, operators and lenders. The following is a representative sample of views expressed during the past several months, as well as our regular review of various industry publications.

Dealership Marketability Trends

Whenever we ask a car salesperson about the industry, without solicitation they begin their answer by discussing the Internet, and customers we see walking the showrooms are as focused on their smartphones as they are the vehicles.

- Customers are “showrooming” dealers, meaning going to a dealership to see a car and then looking online for the best deal - **often before they have even left the dealership!**

“If dealerships are serving mainly as a delivery point in these transactions, do they need to be multi-million dollar facilities requiring an image upgrade every few years?”

- Not everyone agrees that a virtual reality will continue to compromise the importance of physical dealerships. Some dealers say completing a car transaction online is “years away” because valuing a trade-in, arranging financing and complying with regulations make it too complex.
- Lenders, largely blamed for worsening the last downturn by not making credit available, are now helping fuel the strength of the current market with **relaxed lending standards** for both dealership properties and vehicles themselves.
- Industry consolidation continues, with large dealerships increasing their presence. Unless it’s a rural area, “The days of the Ma and Pa entering this business” are “effectively over.”
- Dealerships in rural areas and small towns can be hard to market, even when they are performing well. Automotive News reports, “The hard part is finding good people. And a lot of these **GMs don’t want to live in these little communities.**”

The Rise of Mobility Services

As most vehicles are in operation less than 5% of the time, vehicle sharing could represent an opportunity for significant savings for consumer.

“The idea that maybe you don’t have to own a car if you only need one occasionally may catch on, just like time-sharing caught on in real estate.”

Mobility services include ride hailing services such as Uber and Lyft, which are increasingly expected to be based on fleets of autonomous vehicles. As a result, some analysts believe that personal car ownership has peaked in the U.S., or will shortly, and fleet customers do not need highly visible well-appointed retail stores.

“I worry a lot about the dealers.”

Technology’s Impact on Shopping Habits

While tensions grow between manufacturers and dealers, **the balance of power is shifting to consumers** - thanks to the internet.

- Internet-savvy consumers often find their cars online and when they show up at the dealership they know more than the sales people. As a result, **the need for a physical trip to a dealership is a less important part of the car-buying process than ever**
- Automotive News reports that auto industry leaders say dealerships are now within a year or two of being able to complete **an entire vehicle transaction online**. (That includes pitching finance and insurance products and getting electronic signatures on key documents. There are even online leasing apps popping up, too.)
- The intermingling of technology in the auto-buying process will put further **pressure on mom-and-pop dealers** who can’t afford the investment needed to keep pace.
- While online sales are growing, consumers still find shopping in a dealership to be “an emotional experience”, says one dealer. “We don’t want to take that away from them. This [buying a car] **isn’t like buying a five-dollar case for an iPhone.**”

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Risk Factors

- Online sales initiatives are underway that will result in some customers never even visiting the physical dealership property.
- Autonomous vehicles could decrease in road accidents by up to 80%, which could severely impact the significant revenue generated to dealers from parts and repairs.
- Vehicles that are autonomous are likely to drive themselves home after purchase, and drive themselves to be serviced. A reduction in personal interaction with the customer would reduce the chance for the sale of additional products and services at the dealership - and ultimately limit the usefulness of having a dealership property.
- It is growing increasingly difficult for small operators to compete with the larger dealership groups.
- "Facility improvements is the biggest risk out there" (see Real Estate Trends).

"It can be either a very scary or a very exciting time to be a car dealer."

Outlook

- Long-term risks aside, **right now the market as a whole is on firm footing.**
- 2017 should look a lot like 2016, which is good for most auto dealers and auto dealership properties.
- NADA expert and industry consultant Glen Mercer forecasts that the number of U.S. dealerships will shrink

to around 16,500 in 2025 (down from about 18,000 today).

- Mercer also sees the trend of steady but slow consolidation of store ownership continuing with a pool of 6,500 owners by 2025 (down from 8,000 today).
- Driverless cars and/or completing purchases online could eventually impact car-buying habits to such a great extent that **the entire auto dealership real estate model could be affected.**
- Small dealerships in small and/or rural markets should continue to appeal to mom-and-pop operators; while their numbers are dwindling, mom-and-pop operators are not going away.
- Like all real estate, the outlook for auto dealerships will continue to be property-specific, with their marketability and valuations influenced by:
 - Job growth
 - The microeconomic conditions of their respective location
 - Continuously evolving design standards
 - Factory Image Program risk

2016 Auto Dealership Property Transactions

Below is a representative sampling of information from 2016 transactions tracked by *Greystone Valuation Services*.

Sampling of Notable Auto Dealership Transactions

Brand(s) Marketed/Metro Area	Price/ Date	Building Area (SF)/ Year Built	Land Area (AC)	Price/SF
Confidential (Luxury, Foreign) Jacksonville, Florida Metro Area	\$13,500,000 April 2016	48,883 2008	10.93	\$276.17
<p>Property Notes: Traffic count of 33,000 VPD (vehicles per day). "Dealership row" location with a high density of dealerships in the area. Corner site; no traffic light. New construction activity in the area includes a similar high-end dealership. Demographics (5-mile radius): median income, \$45,451; population, 157,406. Land in the area typically sells for about \$10.00/SF - \$13.00/SF. Attractive masonry and EIFS building with high-end finishes and a primarily single-story design. Approximately 69% of the building represents finished area showroom and office area. Service areas are air conditioned. Fully sprinklered. Included in the net rentable building area is a 2,608 SF parts department mezzanine with a parts elevator. In addition to net rentable building area, there is also a 5,088 SF canopy used for vehicle drop-off. Modern design and appearance; OEM compliant.</p> <p>Transaction Notes: The sale was in conjunction with a portfolio of other dealership properties. However, the price was determined for each based on separate appraisals. Otherwise, typical sale conditions for a new vehicle dealership (i.e., the property was not exposed to the market and the sale of the real property was in conjunction with the sale of a dealership enterprise).</p>				
Kia Dallas-Fort Worth-Arlington, Texas Metro Area	\$7,900,000 February 2016	62,062 2002	11.012	\$127.29
<p>Property Notes: Traffic count of 145,142 VPD. Low density of dealerships in the area. Immediate area has a generally commercial and industrial character. Median income (5-mile radius): \$75,071. Moderately attractive steel and block with typical finishes and a one- and two-story design. Approximately 30% of the building represents finished area showroom and office area. Service areas are not air conditioned. Modern design and appearance; OEM compliant.</p> <p>Transaction Notes: Typical sale conditions for a new vehicle dealership (i.e., the property was not exposed to the market and the sale of the real property was in conjunction with the sale of a dealership enterprise).</p>				
Confidential (Mid-priced, Domestic) Jackson, Mississippi Metro Area	\$7,400,000 February 2016	51,998 2006	10.78	\$142.31
<p>Property Notes: Interstate highway frontage road "dealership row" location with a traffic count of 114,000 VPD. High density of dealerships in the area. Demographics (5-mile radius): median income, \$37,486; population, 200,263. Moderately attractive concrete block, metal and EIFS building with 16' ceiling heights in the showroom 23' ceiling heights in the service area. Approximately 34% of the building represents finished area showroom and office area, and approximately 90% is air conditioned. Fully sprinklered. The service area includes an automated car wash, 34 service bays, and a drive-thru quick lube service area. Fairly modern design and appearance; however, the buyer expected a re-imaging project for the front truss of the building to be required within one year of the sale (anticipated cost of \$300,000 to \$500,000).</p> <p>Transaction Notes: The property was not exposed to the market and the sale of the real property was in conjunction with the sale of a dealership enterprise (typical of a new vehicle dealership sale). The buyer reported that there were "extenuating circumstances" that affected the price paid for the real estate and that he believes the appraised value of \$9,170,000 (\$176.35/SF) was more indicative of the value of the real estate.</p>				
Nissan Seattle-Tacoma-Bellevue, Washington Metro Area	\$7,350,000 June 2016	21,860 1986	3.21	\$336.23
<p>Property Notes: Traffic count of 34,000 VPD. Moderate density of dealerships in the area. Median income (5-mile radius): \$68,832. Moderately attractive enamel steel and aluminum siding building with typical finishes. Approximately 33% of the building represents finished area showroom and office area. Service areas are not air conditioned. Fully sprinklered. There is a second floor (3,600 SF) comprised of office space and a parts mezzanine. Modern design and appearance; OEM compliant.</p> <p>Transaction Notes: Typical sale conditions for a new vehicle dealership (i.e., the property was not exposed to the market and the sale of the real property was in conjunction with the sale of a dealership enterprise). The price was based on an independent appraisal.</p>				

2016 Auto Dealership Property Transactions

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Sampling of Notable Auto Dealership Transactions

Brand(s) Marketed/Metro Area	Price/ Date	Building Area (SF)/ Year Built	Land Area (AC)	Price/SF
Ford Chevrolet Buick GMC Rural Market in Tennessee	\$5,200,000 June 2016	27,924 1997-1998	4.84	\$186.22
<p>Property Notes: Traffic count of 23,430 VPD. Adjacent to a Walmart Supercenter, but with no other car dealerships in the immediate vicinity. Demographics (5-mile radius): median income, \$37,759; population, 27,730. Three separate buildings: Chevrolet Buick GMC Dealership Building (12,760 SF); Former Used Car Dealership Building (1,350 SF); Ford Dealership Building (13,814). The Former Used Car Dealership Building is 100% finished and now used as office space. Metal and stucco exteriors and attractive finishes. Approximately 50% of the building area represents finished area showroom and office area. Service areas are not air conditioned. The buildings are not sprinklered. No manufacturer requirements at the time of purchase, and none expected in the near: "because we are in a small-town market, we don't usually anticipate sudden manufacturer imaging requirements". However, approximately \$40,000 to \$50,000 (\$1.43/SF to \$1.79/SF) in repairs were needed after sale transpired.</p> <p>Transaction Notes: Typical sale conditions for a new vehicle dealership (i.e., the property was not exposed to the market and the sale of the real property was in conjunction with the sale of a dealership enterprise). The buyer did not analyze the value of the real estate internally, and relied on the seller's allocation (which was then validated by an independent appraisal).</p>				
Buick-GMC Oxnard-Thousand Oaks-Ventura, California Metro Area	\$5,050,000 June 2016	21,121 1988	1.00	\$239.10
<p>Property Notes: Traffic count of 37,000 VPD. High density of dealerships in the area. Good commercial location. Median income (5-mile radius): \$74,624. Attractive concrete block construction with nice showroom finishes. Approximately 50% of the building represents finished area showroom and office area. Included in the net rentable building area is a parts department mezzanine. Modern design and appearance; OEM compliant. Commenting on the market, the buyer's broker reported it as "good", with "not a lot available out there right now."</p> <p>Transaction Notes: Arm's-length transaction with the price reflecting real property only.</p>				
Confidential (Mid-priced, Foreign) Birmingham-Hoover, Alabama Metro Area	\$4,625,000 August 2016	27,976 2007	5.00	\$165.32
<p>Property Notes: Interstate highway exposure with a traffic count of 44,080 VPD. Corner site; no traffic light. Low density of dealerships in the area. Demographics (5-mile radius): median income, \$38,309; population, 42,123. Land in the area typically sells for about \$4.00/SF - \$5.00/SF. Moderately attractive construction with enamel steel, pre-engineered metal panels and typical finishes. Approximately 33% of the building represents finished area showroom and office area. Service areas are not air conditioned and have 16 service bays and a drive-thru lane. The parts department and parts mezzanine (1,950 SF) are air conditioned; the total ratio of air conditioned space is approximately 49%. Fully sprinklered. While maintenance is reported to be adequate for a new vehicle dealership, and no compliance issues were known, its appearance is not as new as some dealership properties of similar age.</p> <p>Transaction Notes: A potential buyer approached the owner and an agreement was made to sell the property at a price determined by a process using appraisals developed by MAI's. The property had not been exposed to the market. The sale of the real property was to be in conjunction with a dealership enterprise, as is common for sales of operating dealership properties, with the other dealership assets being sold as part of a separate agreement. After the price negotiations were complete, another party exercised their right of first refusal and purchased the property under those terms.</p>				
Confidential (Mid-priced, Domestic) Rural Market in Illinois	\$4,500,000 Current Contract	51,505 1973-2002	12.0003	\$87.37
<p>Property Notes: Traffic count of 8,600 VPD. Corner site; no traffic light. More than 30 miles from the nearest interstate highway in a somewhat rural community. Few competitive dealerships in the area, and those that exist have a dated appearance with no obvious indications of significant capital improvements or updating. Demographics (5-mile radius): median income, \$37,801; population, 28,750 (and declining). Land in the area typically sells for less than \$2.00/SF. Three separate buildings: New Dealership Building (33,211 SF); Used Dealership Building (10,230 SF); Collision Center (8,064 SF). Metal and stucco construction with average to good finishes for a tertiary market. The New Dealership Building has a parts mezzanine not included in the net rentable area (due to its functional limitations). Approximately 17% of the building represents finished area showroom and office area. Service areas are not air conditioned. The New and Used Dealership Buildings are sprinklered. Manufacturer-required renovation was completed in 2014; no significant capital improvements planned or needed. The recent improvements were a cosmetic re-imagining/remodeling project consisting of exterior reface and an interior remodel of New Vehicle Dealership Building showroom at an approximate cost of \$900,000 (including furniture). Blacktop was resurfaced and a new membrane roof installed over the service drive at a cost of \$27,000.</p> <p>Transaction Notes: Typical for a sale of a new vehicle dealership property, the property was not exposed to the market and the sale of the real property is in conjunction with a dealership enterprise. The price for the real property was developed using an appraisal, and was then negotiated further by the parties involved.</p>				

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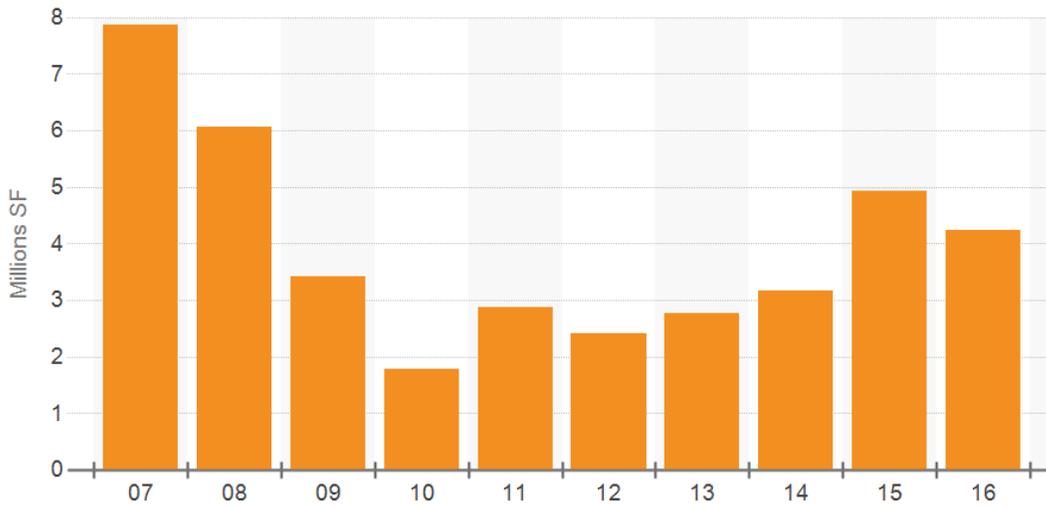
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Auto Dealership Construction Cost Trends

Auto Dealership New Construction Deliveries



New construction deliveries in 2016 lagged the preceding year, despite predictions to the contrary, with activity still well below pre-recession levels.

Source: CoStar

Criteria: Auto dealership properties 10,000 SF+

Below are some examples of costs for specific projects either underway or recently completed.

Recent Auto Dealership Cost Comparables			
Vehicle Price Point	Building Size	Cost/SF-Building*	Improvement Cost/SF*
High-End/Luxury	18,817 SF	\$212.29	\$248.98
High-End/Luxury	78,830 SF	\$179.62	\$224.96
Mid-Priced	46,537 SF	\$178.81	\$240.48
Mid-Priced	36,990 SF	\$168.67	\$187.05
Economy	25,882 SF	\$167.90	\$229.82
Mid-Priced	17,042 SF	\$150.67	\$190.39

A **shortage of skilled labor** and **worksite compliance requirements** have put upward pressure on costs.

*Excludes land, and is adjusted to reflect local variations in cost

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What's Ahead

For what's ahead, we looked to the auto dealership construction experts at TallyCM, who shared that many industry leaders predict that 2017 will be a strong year for the industry. The economists at Dodge Data & Analytics predict 5% growth in the value of construction starts in 2017.

TallyCM expects to see the following automotive facility construction space trends for 2017:

- Skilled labor shortages are present and General Contractors face pressure to retain experienced tradesman
- Higher land costs in urban and metro markets lead operators to build multi-storied facilities
- Dealers are designing larger service areas and new bays to accommodate electric vehicles
- Continued growth in the Western states like Texas, Utah, Colorado and California
- "Ground up" facility cost per square foot increase of 4.5% - 6% vs. the prior year
- OEM's are enforcing facility design plans and have set expectations for compliance

TallyCM provides owner's representation and general construction management services for the automotive industry. TallyCM's core services include:

- Placement of TCM certified construction managers to oversee program/projects.
- Complete owner's representation through the planning, design, construction and post construction phases of a new build and re-image projects.
- Long term facilities maintenance service contracts and warranty assurance products.
- Site assessments and property inspection reports for Buy/Sell scenarios.

TallyCM has experience with a wide variety of manufacturers and has built a proven track record with established groups like Larry H. Miller Auto Group, Penske Automotive Group, Earnhardt Auto Centers, Pierce/John Elway Automotive, Mike Shaw Automotive, Avondale Automotive Group, Hardin Automotive and many more dealership groups.

For more information about TallyCM visit www.TallyCM.com.



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