

December 13, 2018

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# **Trade Disrupted (Multi-part Series): Disruptors and Technology Will Bring Transparency to the Vehicle Trade-in Market**

- Investment capital is flowing into start-ups that give car owners access to more accurate appraisals and new channels for realizing the value of their vehicles.
- Artificial intelligence (AI) is improving inventory management by incorporating the unique vehicle, market, and seller characteristics that influence the retail price of every used car.
- The combination of start-ups and AI could impact dealer margins, remarketing channels, and potentially the role of wholesalers.

## Disruptors and Technology Will Bring Transparency to the Vehicle Trade-in Market

*For nearly two decades, car buyers have been able to search online for exactly the make and model they want, view photos and condition information, and see the actual price a dealer was willing to sell a car for, but the critical piece of the car buying process that remained obscure was the appraisal value of the trade-in vehicle. Online consumer-facing tools could only provide averages for trades, which meant they could be very high or very low, and were almost always inaccurate. Furthermore, unlike new cars, where every unit of the same make, model, and trim level is identical, used cars are subject to many more factors that affect their value. For example, a franchise dealer appraising a same brand car is likely to pay more because it knows its retail customer will pay a premium for a car that is sold by a same make dealer. A car in excellent condition with a complete maintenance history might deserve a higher value whereas customer installed accessories could add or subtract value. None of these important factors, and others, played into the valuations provided by online tools, which resulted in customer frustration and distrust of dealers that presented a lower appraisal value. We are, however, in the early stages of an evolution in trade-in options for consumers that will give them greater control over the process, including more channels through which to obtain market-based values and sell their vehicles.*

CarMax branded itself as the car dealer that would buy any vehicle at a guaranteed price, regardless of whether or not the owner purchased a replacement. Few people sought other estimates given the inconvenience and time it took to appraise the car. This model provided CarMax with profitable inventory for its retail lots, and for vehicles that were unsuited for retail, it provided wholesale inventory for CarMax's auctions. According to recent data, CarMax acquires about 40% of its retail inventory through the appraisal process; the remaining vehicles are wholesaled through its own auctions. In the fiscal year ending March 2018, the used car retailer sold 408,509 wholesale units with an average per unit profit of \$926 – nearly four times the wholesale profit of a typical franchise dealer. But consumer acceptance of modern online trade tools and appraisal services is now bringing transparency to the trade-level, and *all* car dealers (including CarMax) are affected. Thus, CarMax's recent decision to launch more app-based appraisal tools and other online technology is being driven by the consumer-facing technology evolution that is occurring in automotive retail.

Consumer-facing services that provide trade-in estimates have been around for decades. When these estimates were too high, dealers couldn't honor them, which led to frustrated customers and consumer distrust of dealers. These services were based on wholesale market averages and limited information from owners, and failed to consider that every vehicle had its own value to a specific dealer. These appraisals did not reflect the vehicles' unique characteristics (trim-level, options), condition, regional preference differences, local demand and supply, or factors about the acquiring dealer (e.g., franchise, the dealership's current inventory, etc.). But, today, consumer-facing trade-in offerings are integrating detailed inspection photos and vehicle options while also analyzing other data — such as real-time market demand and supply. They are able to give owners more accurate valuations for their vehicles or the means for consumers to determine that for themselves by accessing dealers directly through consumer-to-business (C2B) auctions.

Start-up tech companies are recognizing the opportunity to connect directly with car owners and to control the remarketing experience. There are dozens of companies and services that will buy cars directly from vehicle owners. Some of these services are established and well-known, like Accu-Trade (R. Hollenshead's company), AutoTrader's Trade-In Marketplace, or CarMax's app-based appraisal

service. Other entrants, like Shift Technologies or CarLotz, have emerged and offer consignment models that attempt to maximize the retail selling-price of vehicles by selling them to other consumers on behalf of the vehicle owner. C2B auction start-ups, like Swap Motors and DealerStrip, auction consumer cars directly to dealers. There are also other trade-related apps and offerings emerging that use photos and artificial intelligence (AI) tools to set wholesale values for each vehicle. The resulting transparency from these technologies has all but eliminated the dealer’s ability to “steal a trade” by providing consumers with offers that are both competitive and more accurate.

**Exhibit 1: Vehicle Trade-In Appraisal Landscape (U.S.)**



**Note:** The vehicle trade-in landscape includes multiple vendors, each with their own value proposition. The landscape depicted above represents companies from the B2C, B2B, and C2B spaces. This graphic is non-exhaustive.

Outside of consumer-facing propositions, in-dealership innovation is also occurring. Before a retail deal with a vehicle shopper has closed, companies like TradeRev and The Appraisal Lane allow their participating dealers to receive a wholesale offer for the trade. The services provide binding bids from other dealers, remarketing companies, and nationwide wholesalers that are willing to buy the specific vehicle based on the details and photos provided by the retail dealer. Thousands of vehicles are already being remarketed this way, and it’s allowing dealers to offer a true market value for a customer’s trade while eliminating the risk of overpayment. Also, in many cases, dealers show the wholesale offers from these B2B tools to their retail customers, thus bringing more transparency to the trade-in process and giving consumers extra assurance that their dealers’ trade-in offers are competitive. In addition, as these services scale nationwide, some B2B companies are expanding their offerings directly to consumers, allowing them to sell their cars to dealers via the C2B model.

Artificial intelligence tools are also bringing innovation to the trade-in process by allowing dealers to more accurately determine future retail prices for trade-in vehicles as well as the number of days required to sell them. Used car inventory management and pricing tools have undergone improvements that now enable dealers to estimate the profit potential of any trade and better determine its value, even before it enters their inventory. These tools factor in market supply and demand, a dealership’s inventory turn rate, gross margin, and franchise as well as a variety of computer-learned factors that are analyzed to provide accurate predictions for dealers.

New offerings by incumbents and start-ups are bringing efficiencies to the trade process by removing friction for consumers and maximizing their vehicles' values. The offerings also remove risk for dealers by providing them with competitive and guaranteed vehicle appraisals as well as accurate predictions for retail prices and "time on the lot." As these tools continue to scale nationwide, dealers will no longer rely on used car managers to set trade-in values, but it also means that dealerships that aren't embracing these technological shifts will soon be at a disadvantage.

### **Next in Trade Disrupted: Volume Contraction for Wholesalers and Physical Auctions?**

As the wholesale market for dealer trades becomes more efficient, it will impact wholesalers and physical auctions. Traditional wholesalers that buy dealership trades will have less access to inventory as unwanted vehicles once bought from dealers will increasingly be sold to nationwide wholesalers and other dealers via virtual and real-time auctions. Similarly, fewer dealer consignment units will go to physical auctions as trade units will be sold dealer-to-dealer instead.

The impact of this shift for wholesalers and physical auctions will be explained in the next update of our multi-part series on the trade-in market.