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**A**re certified pre-owned vehicles reshaping the U.S. market?

While new vehicles still outsell them by a wide margin, CPO cars and trucks, which undergo a 100-plus-point manufacturer-mandated inspection and usually are between 4-to-8 years old with relatively low miles, appear poised to take off in the coming years.

“The thing that continues to amaze me, and has for years, is month after month after month, the industry is setting records and manufacturers are setting

records, in the number of certified pre-owned cars they’re selling,” says Ricky Beggs, owner of Beggs on Wheels, a diminished-value vehicle consultancy. “You think after a while you can’t continue to get better and better and better, but that’s a sign of just more confidence in that certified pre-owned car.”

Sales of certified pre-owned vehicles have been on an 8-year hot streak in the U.S., Cox Automotive data shows, going from 1.528 million in 2009 to 1.835 million in 2012 and reaching 2.642 million last year.

Many factors are fueling the

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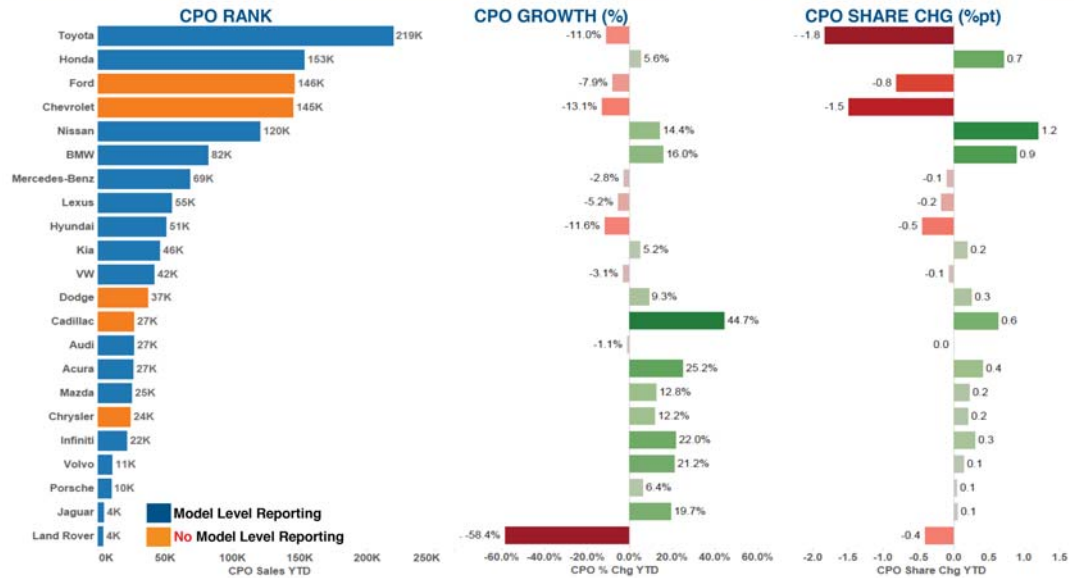
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# THE BIG STORY

## CPO Sales and Share by Brand as of July 2017 YTD



Source: Cox Automotive, Autodata/Motor Intelligence

rise of CPO, but a major one is the growing popularity of leasing. This is leading to a steady supply of vehicles coming back to dealer lots every two or three years with low miles on the odometer and little in the way of wear and tear.

The deluge of off-lease vehicles hitting the U.S. market already has begun, says Cox’s Mark Strand, director-Economic & Industry Insights, with 3 million off-lease vehicles returned last year, up 500,000 from 2015. This year, off-lease returns are poised to hit 3.6 million. That number could climb to 3.9 million in 2018

and 4.3 million in 2019. Cox estimates 4.6 million vehicles will be returned in the U.S. by lessees in 2020.

Can the CPO sector absorb all these vehicles? Strand thinks so, based on the fact the incremental volume of off-lease vehicles hitting the market won’t be as high in coming years as it has been the past two years. The big percentage growth in off-leased vehicles depressed used-car prices last year and early this year, but he foresees a recovery.

“When you look at the Manheim Used Vehicle Value Index, which



is more adjusted for mix and mileage and we think more accurately reflects on an adjusted basis what's happening out there, vehicle values are not tanking," Strand says.

"So our conclusion is the market did absorb the major influx of off-lease volume without a crisis," he says.

Despite those rosy projections, CPO sales are up just 0.6% through July, with Cox blaming good deals available on new vehicles and the fact most leased vehicles being returned are cars and not light trucks, especially trendy CUVs.

In the span of the average 2-to-3-year lease term, car share as a percent of total light-vehicle sales has dwindled from 47% in 2014 to 43% in 2015 and 39% in 2016, *WardsAuto* data shows.

The situation should rectify itself in coming years because CUV leases are rising.

"In the future, the profile of off-lease is going to more reflect consumer demand (for CUVs)," Strand says. "That will come into alignment, but that's going to

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**Camry seeing reduced CPO share this year.**



take a few more years.”

Eight of the 10 biggest market-share gainers in the January-July period were CUVs, models such as the Honda CR-V, Nissan Rogue, Cadillac SRX and BMW X5.

The biggest losers? Mostly cars, with the exception of one mini-van and two large CUVs. Toyota’s Camry, Corolla and Prius models, Hyundai’s Sonata and BMW’s 3-Series and 5-Series sedans are some of the cars seeing reduced CPO share year-to-date, Cox says.

Strand says off-lease vehicles should continue being a feeder system for CPO, given many American car buyers today have the cellphone mindset: trade

up to new technology every few years.

“We don’t think (leasing) will stay at 30%, but...past 25% (and) close to 30% could be a permanent fixture,” Strand says.

## Warranties a Driving Factor

Another big factor behind growing CPO sales is the warranty. Oftentimes, CPO vehicles boast better factory backing than new models.

“In many, many cases, the warranty on (a) certified car is actually longer than the new-car warranty,” says Beggs. “So that’s



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**Sewell Lexus of Dallas has separate pre-owned facility.**

a confidence-level builder (for a customer).”

Lexus, one of the first brands to participate in CPO back in the early 1990s, last year revamped its U.S. program, going to a 2-year/unlimited mileage warranty from a 3-year/100,000-mile (160,934-km) warranty.

“We really looked at the benefits to the customer and we went to an unlimited-mileage warranty that’s stacked on top of the remainder of the original-equipment warranty, so you’ve got that extension,” says Eric Shuttee, manager-L/Certified Operations for Lexus.

New Lexuses come with a 4-year/50,000-mile (80,467-km) guarantee, so a CPO customer potentially could have up to six years of coverage.

Dan Frogge, assistant general manager for Sewell Lexus of Dallas, the leading seller of Lexus CPO vehicles in the U.S. 17 years running, says the change has been beneficial.

“Many people believe an L/Certified pre-owned Lexus is better than a new car...because you get unlimited mileage,” he says.

Mercedes-Benz claims to have been the first “non-specialty man-





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**BMW X5, one of CUVs gaining CPO share this year.**



ufacturer” to provide an unlimited mileage warranty for CPO vehicles when it did so in 2014.

Alan Katz, general manager-pre-owned, remarketing and fleet operations for the brand in the U.S., says the luxury make – the No.2 best-selling CPO luxury brand in the U.S. through July, with 69,000 sales per Cox data – also offers its CPO customers the ability to extend coverage through factory-backed extended limited warranties, “which also have no mileage limitation.”

The Mercedes unlimited warranty also is stacked on top the remainder of the new-car warranty, but is good for just one year

vs. two for Lexus.

BMW has a 6-year/100,000-mile warranty from the date a vehicle was first sold, as well as a \$50 deductible, while Lexus and Mercedes require no deductible.

The less-generous coverage apparently hasn’t hurt the brand. BMW is the No.1-selling CPO luxury marque in the U.S., with 82,000 sales through July, up 16.0% from like-2016.

When asked about warranties and other coverage perks, Kevin Rustad, CPO sales manager for North America, says BMW is at work on enhancements to its program that will be announced soon.

While luxury brands used to



**Multi-point maintenance check by Lexus service tech part of CPO experience.**



comprise the entirety of CPO sales in the U.S., non-luxury makes now command more than half the market, with five brands alone – Toyota, Honda, Ford, Chevy and Nissan, taking a 52% CPO share this year with nearly 800,000 units sold. For these brands, warranty terms naturally are less generous.

For instance, Toyota, Honda and Chevrolet, the three best-selling CPO makes in first-half 2017, all offer 12-month, 12,000-mile (19,312-km) bumper-to-bumper

warranties. While Toyota and Honda include 7-year/100,000-mile powertrain warranties, Chevy offers a 5-year/100,000-mile guarantee. The Toyota and Chevrolet warranties take effect the day the vehicle is sold.

Beyond warranties, many brands, luxury and non, also offer perks such as free loaner cars and 24-hour roadside assistance.

With its program update last year, Lexus now covers the first four factory-scheduled maintenance services for two years or



**CPO vehicle deals likely to be made in as nice an environment as new-vehicle sales.**



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20,000 miles (32,187 km).

“So if they bought a car with say 61,000 miles (98,000 km) and that car was due (for) the 65,000-mile (105,000-km) maintenance, they would get the full maintenance – not just an oil change, not just a tire rotation,” Shuttee says, adding buyers also get major scheduled maintenance such as 30,000-, 60,000- and 90,000-mile (48,000-, 97,000- and 145,000-km) checkups.

“As you know all the luxuries have upped their game, so we saw that trend,” he says. “I took

over right at that change. The previous (manager) wanted to make sure we were ahead of the game.”

## The Used Experience, Elevated

It used to be that buying a used vehicle was a second-class experience. Instead of a shopping in a big, swanky new-vehicle showroom, buyers were forced to complete a deal in a tiny, battered, backlot building or a trailer.



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A sample inventory search on Mercedes' CPO website shows how finely results can be sliced.

The screenshot shows a search interface for Mercedes-Benz Certified Pre-Owned (CPO) vehicles. At the top, there are tabs for 'New Inventory' and 'Certified Pre-Owned Inventory', with the latter selected. A search radius of '50 miles' is set, showing '48075' total vehicles. Filter buttons include 'Year & Price', 'Body Style & Class', 'Model', 'Color', and 'Mileage & Drive Train'. A search filter for 'C300 4MATIC Sedan' is active, with a 'Clear All' button. Below the filters, it says 'Last updated on 8/18/2017' and 'Sort by: Distance'. A summary bar shows '12 Vehicles' for the selected filter. The main result is a 'C300 4MATIC Sedan' with a 'CPO' badge. It includes a photo of the car, a 'Save to Favorites' button, and the following details:

<b>Specifications:</b> Year: 2015 Miles: 13,681 Miles Exterior: Black Interior: Black MB-Tex VIN: 55SWF4KB6FU028666	<b>Includes:</b> <ul style="list-style-type: none"><li>• Heated Front Seats</li><li>• Gloss Black &amp; Aluminum Trim</li><li>• LED Headlamps</li></ul>	<b>Located at:</b> Mercedes-Benz of Bloomfield Hills (248) 644-8400 7 miles from 48075	<b>\$37,993</b>
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But that scenario is mostly a thing of the past, especially when it comes to CPO.

Frogge says Sewell Lexus has a large, dedicated pre-owned showroom just down the street from its new-vehicle store.

“We actually have a separate pre-owned facility,” he says. “It’s a block away from our main showroom, complete with its own service technicians and all that.”

However, he says CPO deals can be made in the new-vehicle showroom and vice versa, without a buyer needing to change salespeople, as all of Sewell’s sales staff is trained to sell both.

Mercedes’s CPO models sometimes are sold in a dedicated facility, Katz says, depending on a dealer’s location and CPO volume, but many are retailed in a section of a Mercedes’ new-vehicle showroom.

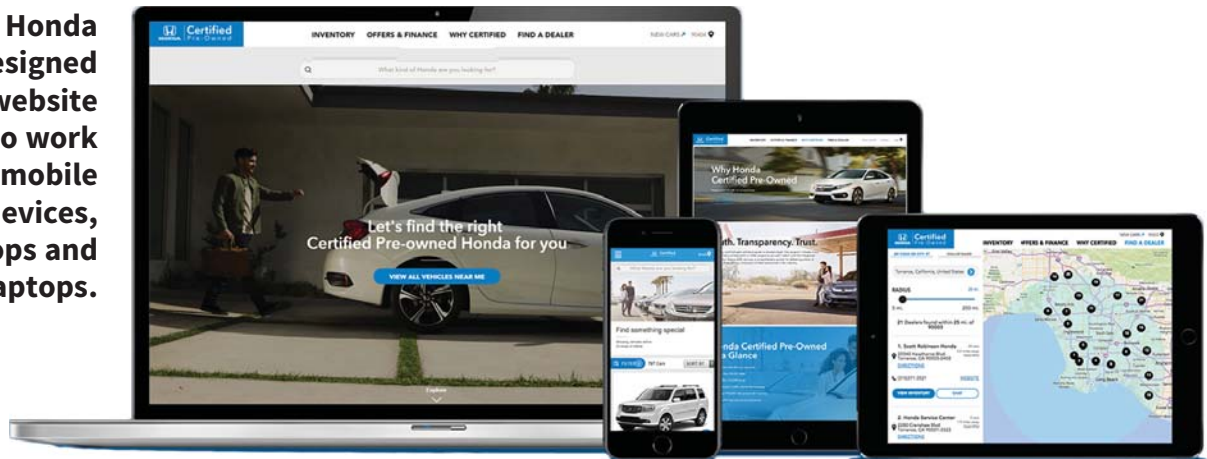
“Atmosphere is important in the sales of all Mercedes-Benz vehicles, whether new or CPO,” he says. “Our customers expect a luxury experience, which includes state-of-the-art facilities.”

Audi takes it a step further, with “most” of its dealers typically having new and CPO vehicles in one showroom, says Thiemo Rusch, vice president-sales and



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**Honda redesigned CPO website to work across mobile devices, desktops and laptops.**



operations for Audi of America.

“A premium sales experience is paramount and creates lifelong Audi fans,” Rusch explains of why the two are under the same roof.

As BMW’s CPO volume grows, Rustad says the brand is encouraging its dealers to have stand-alone CPO buildings, but it isn’t a requirement.

Lexus’ Blake Sturrock, group manager-sales and dealer development, says his brand also allows the dealers to do what is best for their operation in terms of showcasing and servicing CPO units.

But before most buyers even walk into a showroom, they’ve already done their research online. That’s one reason Honda, the No.2-selling CPO brand through

July, recently redesigned its CPO website.

“The old site information was kept up-to-date, but the functionality and look and feel of the site needed to be brought up to speed with what customers want and need during the shopping process,” says Dan Rodriguez, manager-Auto Remarketing and Certified Pre-Owned at American Honda.

Following a 3-month study, Honda found what CPO intenders want and need above all else is a good inventory search tool. This led Honda to improve the search function – via features such as an inventory alert and the ability to find models by specific traits such as a leather interior or a rearview camera – and de-emphasize its program benefits’



section. Program benefits, previously accessible under a like-named link with expanded text in the middle of the homepage, now can be found under the subhead “Why Certified.”

“Ultimately, we wanted the site to be visually appealing and be able to do what CPO consumers focus on first, which is being able to find inventory easily,” he says.

Honda’s CPO website also now provides a consistent and faultless experience no matter if a shopper is using a mobile device or a desktop. This was important as Rodriguez says Honda’s monthly analytical data shows

most of the site’s traffic is coming from mobile devices.

## Is CPO Hurting New Sales?

With new light-vehicle sales running 3.0% behind year-ago through July, and the aforementioned attractive warranties, plus incentivizing, it begs the question: Is growth on the CPO side coming at the expense of new vehicles?

After all, sales of used vehicles tend to be more profitable for a dealer, with both Honda and Lexus noting their dealers keep their CPO profits after footing the



**Toyota's  
Bob Carter  
says CPO  
supports  
residual  
values.**



JOE WILSSEN'S PHOTOGRAPHY

inspection and certification costs.

But all interviewed say it is unusual for a new sale to morph into a CPO sale, with the opposite being more common.

Says Katz: "We find that many aspirational customers entering the luxury market begin with a CPO vehicle, then move to a new Mercedes-Benz for future purchases. Generally speaking, it is less common for a new-car customer to switch to a CPO product."

At BMW, Rustad says a CPO vehicle sometimes begets another CPO purchase, but more often

is the first step before buying new. Many BMW CPO customers typically are coming to a luxury marque for the first time, he says, with inflow usually from Honda, Toyota and Volkswagen.

"Does CPO affect new-car volume? The pure answer to that is no, it adds to it. It supports the residual values," says Bob Carter, executive vice president-sales for Toyota Motor North America.

Carter adds Toyota incentivizes its dealers to do CPO because the automaker is "in the long-term game."



“When people buy a certified car, the retention rate we have in the service department, and then getting them back for the next purchase, is much higher than a standard used car.”

Lexus also doesn't see new-to-CPO occurring, says Group Vice President Jeff Bracken. However, he believes as long as someone is buying a Lexus, that's a good thing.

“We kind of look at this from the perspective of a balanced operation, so...there's new, but there's also L/Certified and there's pre-owned,” Bracken says. “So from our standpoint, whether the used-to-new is 0.3:1 or 0.5:1 or 1:1, it doesn't really matter because all of it is contributing to a very balanced operation.”

And buyers aren't always choosing CPO for a lower-priced vehicle.

Lexus' Shuttee says typically someone buys a CPO model because they want a better-appointed vehicle at a given price point.

“What we find is the L/Certified buyer may pay almost as much as the new buyer in some instances, and that's because...they're able

to move up a model, so that person who came in looking at an ES (midsize sedan) can afford a GS (mid-large sedan).

“Or what happens even more often is that customer who is looking for an entry-level IS can actually afford more accessories and a better-equipped vehicle.”

Regardless of why people are buying CPO, what's clear is sales will continue to climb, especially once inventory is more slanted toward light trucks.

In one less-aggressive scenario, Cox forecasts U.S. CPO sales could hit 2.730 million this year and reach 2.797 million in 2018.

But using the average growth rate of the past three years, 2.877 million sales in 2017 and 2.995 million by next year is not out of the realm of possibility. **WA**



*This story was written by Senior Editor Christie Schweinsberg.*