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NADA Used Car Guide

# PERSPECTIVE

## Certified Pre-Owned Vehicles: 2016 Market Update

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# Certified Pre-Owned Vehicles: 2016 Market Update

## INTRODUCTION

For the past 20 years, manufacturer-sponsored CPO (certified pre-owned) programs have given consumers a third option for auto purchases in addition to new and used: superior used. The programs were originally designed to protect residual values at a time when unprecedented numbers of off-lease vehicles were scheduled to hit the used market. In order to turn a used vehicle into a superior used one, the steps are straightforward: Inspect and recondition used vehicles to near-new standards, include an extended warranty to provide peace of mind, and treat customers to a new vehicle-like sales experience to prop up used vehicle demand, and by extension, used vehicle prices.

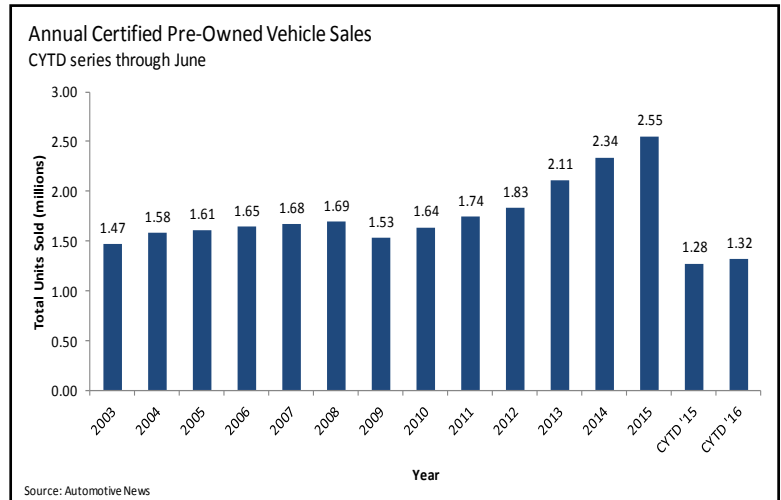
Even though certified pre-owned programs sales have grown substantially over the past several years, it could be argued that CPO’s most important days lie ahead. By weaving together sales and dealership trends along with consumer responses to a recent consumer-facing CPO survey conducted on [NADAguides.com](http://NADAguides.com), this edition of Perspective provides background on the current state of the certified pre-owned market and offers insight to its potential.

## CPO SALES TRENDS

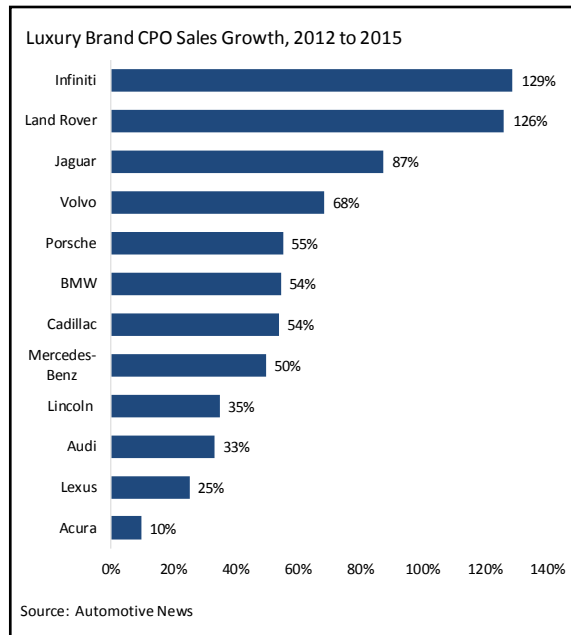
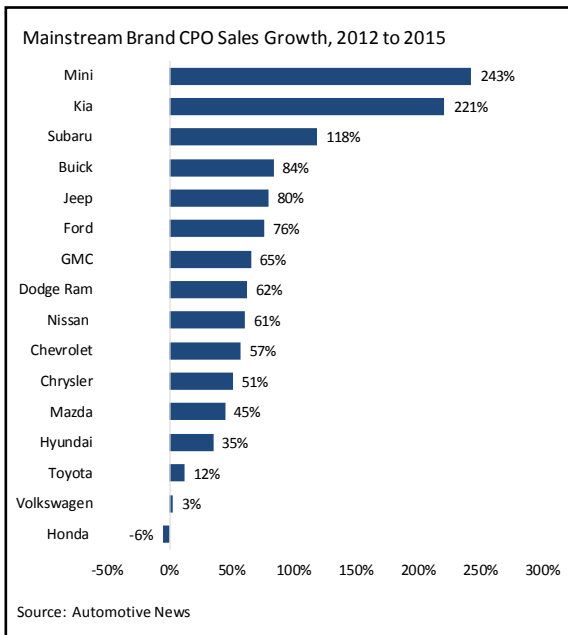
After growing rapidly through its infancy stage at the beginning of the 2000s, CPO sales experienced incremental gains in the years that followed. Hindered by higher costs and limited awareness, the program’s sales increased by only 200,000 units from 2003 to

2007. Deliveries consistently fell between 1.5 to 1.7 million units over the period. However, the unimpressive numbers didn't last much longer.

After languishing for the better part of a decade, CPO sales began to take off in 2011. The rise was partly due to a general auto demand recovery. Increased awareness of — and consideration for — CPO units among the value-conscious post-recession consumer also contributed to the rise. Program sales reached an all-time high of 2.55 million in 2015, which marked a nearly 900,000 unit improvement (54% increase) over levels reached in the years leading up to the Great Recession. Supported by a progressive rise in off-lease supply, CPO sales through the first half of 2016 were up 3.9% to 1.32 million units, which has put them on a pace to set another new record by year's end.



Mainstream and luxury brand certified sales grew at similar rates over the past several years. From 2012 to 2015, mainstream marques rose at a compound annual rate of 11%, while luxury brands saw a 13% increase. Certain brands stand out because of the substantial gains made over the period. Among these are Kia, Subaru, Infiniti and Land Rover. Each brand grew CPO sales by more than 100% — or 200% in Kia's case — between 2012 and 2015. Not coincidentally, each were among the leaders in their respective markets in terms of off-lease growth over the period as well.



Year-to-date, CPO sales growth stands at 4% for both mainstream and luxury brands.

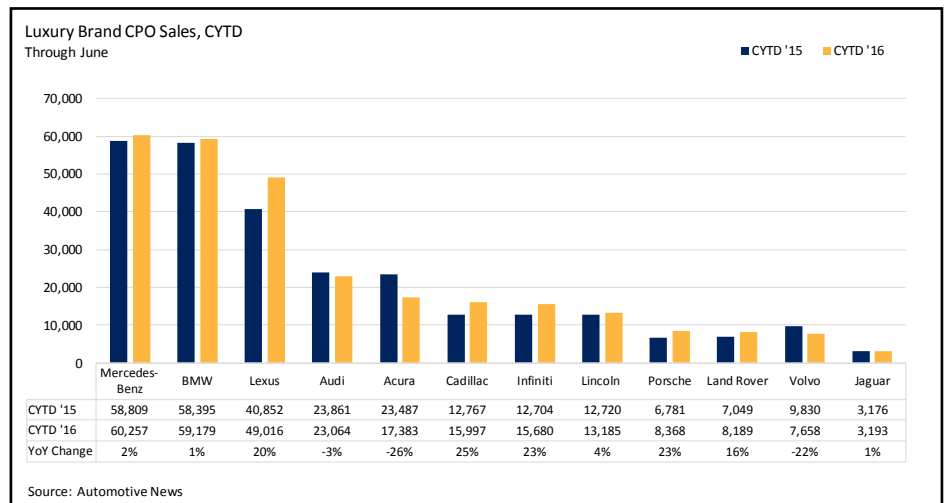
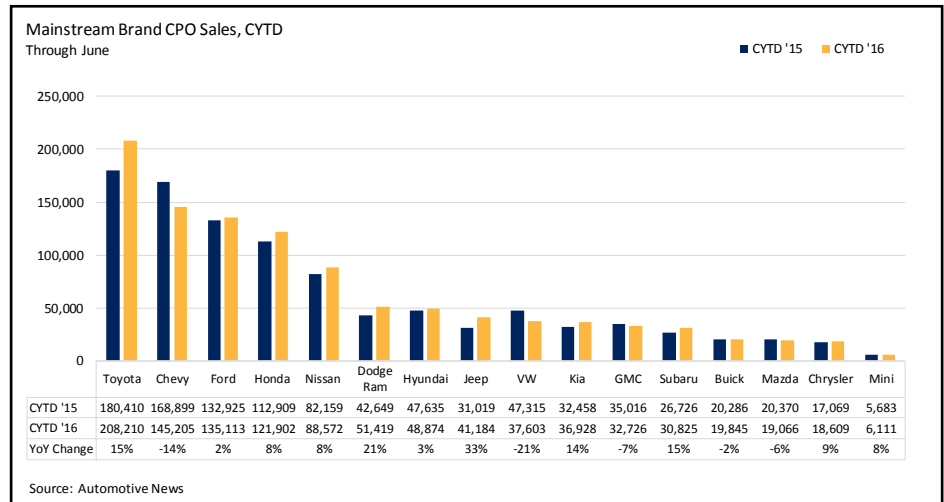
Among mainstream brands, Toyota has sold the most CPO units, but some of its competitors are growing faster. With a 15% sales improvement over the first half of the year to more than 208,000 units, Toyota continued to sell more certified units than any other mainstream brand. In terms of increased sales percentages, however, sales for Fiat Chrysler’s collective Dodge, Ram, Jeep and Chrysler brands have grown 23% YTD — the most among all automakers. With sales up 8% YTD, Honda appears on its way to achieving its first material increase in annual CPO deliveries since 2013. Nissan’s similar 8% rise adds to last year’s substantial 23% increase. By comparison to the success of all the brands above, CPO sales for last year’s second place Chevrolet fell by 14% to 145,205 units through June (sales for GM’s other non-luxury brands Buick and GMC are down as well).

As for luxury brands, Mercedes-Benz remains the segment’s top CPO seller with sales up 2% to 60,257 through June. BMW’s 1% increase placed its 59,000 total just short of Mercedes. The first half of 2015 ended with Lexus trailing Mercedes and BMW by roughly 18,000 units. It should be noted the pronounced 20% increase in sales YTD has narrowed the gap to 10,700.

Other remarkable luxury brand improvements include Cadillac and Infiniti where sales are up by an average of 24%. In contrast to the many positive movements in the luxury market, CPO sales for Acura and Volvo are down 26% and 22%, respectively.

## CPO DEALERSHIP TRENDS

Both NADA Used Car Guide and its owner, J.D. Power, collect transaction-based CPO data directly from manufacturers and franchise dealers. Among other items, the data



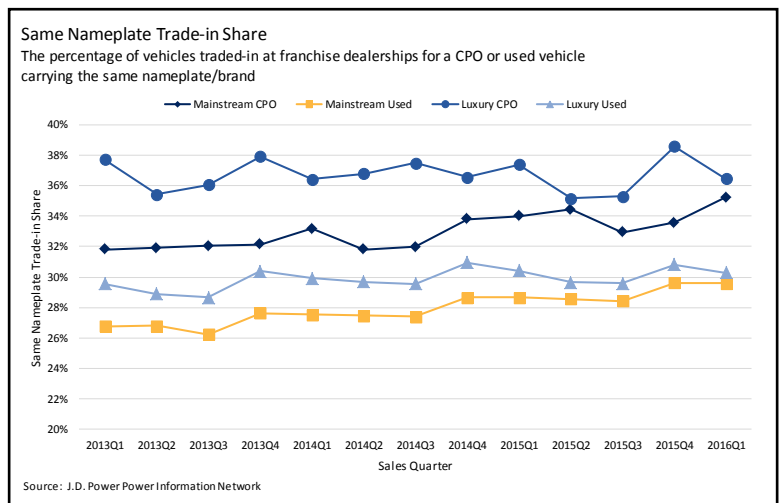
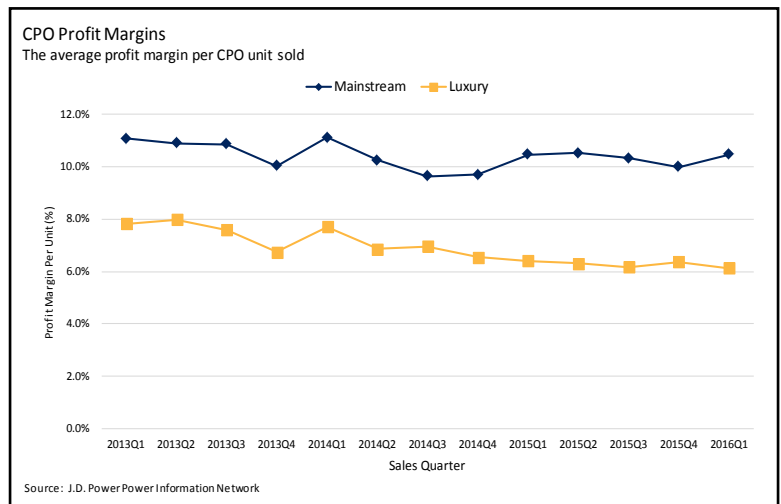
provides important insight into CPO profitability, customer loyalty and premiums paid by consumers for CPO vehicles versus non-CPO used vehicles.

From a profitability standpoint, J.D. Power data shows franchise dealer CPO total profit margins on mainstream vehicles have remained relatively unchanged from Q1 2013 through Q1 2016. Total profit margins for non-premium vehicles have ranged between 9.6% – 11.1% per unit; an average of 10.4%. The total profit margin is comprised of two components: vehicle profit margin (5.6% average) and finance and insurance (F&I) profits (4.9% average).

Compared to their mainstream counterparts, luxury CPO vehicles yielded lower profit margins over the same period. While transaction prices for premium CPO vehicles averaged \$14,687 more than their mainstream counterparts, profit margins for these units ranged between 6.1% – 8% (average of 6.9%) over the period, which is 3.5 points lower than mainstream CPO transactions. While CPO profit margins and F&I margins on the mainstream side of the market are split more evenly, luxury dealers have only experienced average gains of 4.5% and 2.4%, respectively.

J.D. Power data also reveals that customers who purchase CPO vehicles tend to trade in a vehicle from the same nameplate (e.g., trading a used Ford for a certified pre-owned Ford) more often than customers who purchase non-certified used vehicles. Put another way, CPO buyer brand loyalty is stronger than it is for the typical used vehicle buyer.

On average, buyers of mainstream CPO vehicles traded in vehicles from the same nameplate 33% of the time in the first quarter from 2013 to 2016. By comparison, buyers of non-certified used vehicles traded in a same nameplate vehicle 28% of the time, or 5-percentage points less. With a 7-percentage point advantage over used, brand loyalty for luxury CPO buyers was even more significant over the period. Keeping more consumers in the brand fold is critical to the fortunes of automakers and the dealers who represent them.



### CPO Premiums

Certified pre-owned vehicles cost more than their non-certified counterparts. The higher cost is due to the expenses associated with a comprehensive inspection, repairs required to meet manufacturer certification standards (e.g., worn tires replaced, cracked windshield repaired, worn brake pads replaced, etc.) and the bumper-to-bumper extended warranty. Most CPO programs also include roadside assistance and a free vehicle history report. Some even include free scheduled maintenance, which includes services like oil changes, tire rotations, or more.

As for differences in CPO premiums, NADA Used Car Guide concludes that premiums are dictated by four primary factors:

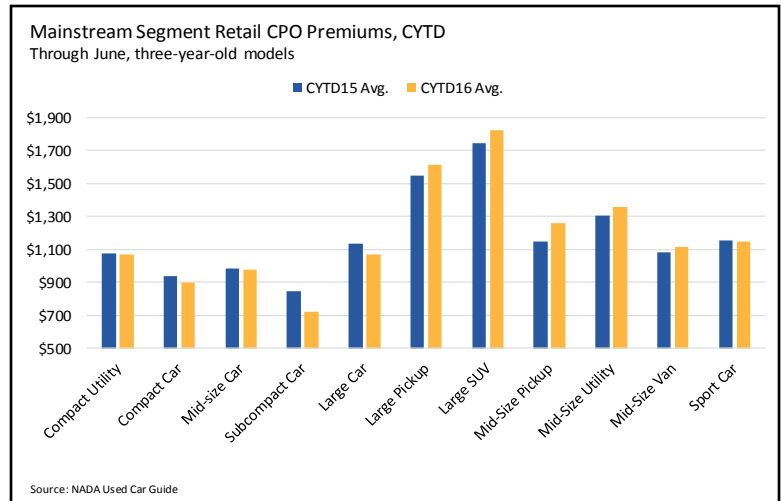
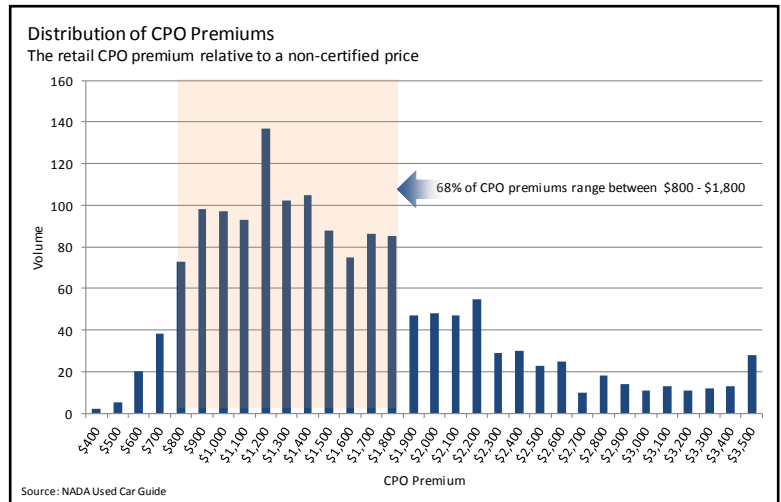
1. Vehicle brand
2. Age
3. Price
4. Competitiveness of a given manufacturer’s CPO program (i.e., length of warranty, mileage allowance and more).

Correspondingly, the above factors and CPO sales data form the basis of NADA Used Car Guide’s certified pre-owned value methodology.

Generally speaking, CPO values are greatest for newer and more expensive models backed by programs that extend bumper-to-bumper and powertrain warranties out the furthest. Values are lower for older, less expensive and less competitive programs.

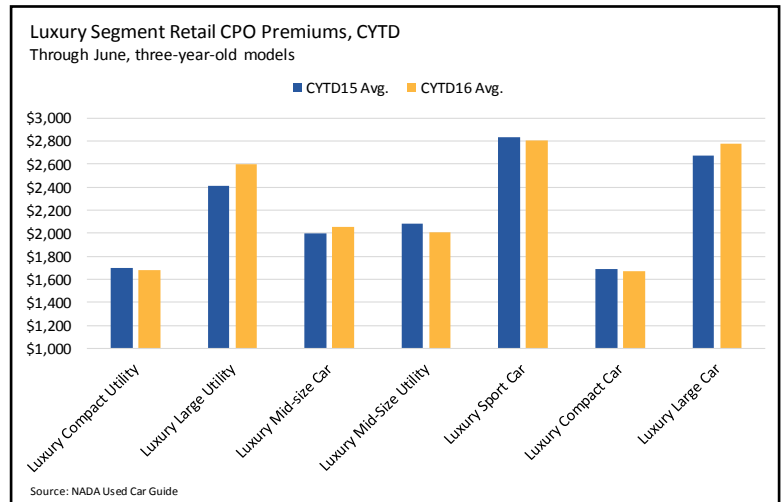
Currently, NADA Used Car Guide’s mainstream and luxury brand CPO premium data indicates 68% of premiums range between \$800 – \$1,800. At the low end of the spectrum, the 2011 model year Smart FORTWO currently has a \$400 premium over its non-certified version. At the high end, late-model vehicles such as the 2015 Porsche 911 currently carry a \$3,500 premium over non-certified versions.

Barring a few exceptions, CPO retail premiums have been fairly consistent year-to-date. For example, three-year-old model CPO premiums for the majority of mainstream segments changed by an average of 3% (plus or minus) over the first half of 2016 versus



the same period last year. The subcompact car and mid-size pickup segments have experienced greater change, however. Subcompact car premiums have fallen by roughly 15%, while mid-size pickup premiums have grown by 10%. Both of these price differences are indicative of each respective segment’s weakness and strength in today’s market.

Similar to mainstream segments, luxury segment premiums have also changed relatively little this year. Premiums for the majority of three-year-old models rose or fell by an average of just 2%. The luxury large utility segment is an exception, as premiums for the group increased by 8% over the period.



## 2016 CERTIFIED PRE-OWNED CONSUMER SURVEY RESULTS

NADA Used Car Guide’s 2016 Certified Pre-Owned Consumer survey was conducted on [NADAguides.com](http://NADAguides.com) from May 27 to June 3, 2016. The multiple choice survey was conducted to assess consumer awareness of CPO programs, future CPO purchase consideration, and the premium (if any) consumers would be willing to pay for a CPO vehicle versus a non-certified used vehicle.

Nearly 3,100 visitors to the site completed the survey. Of those, 81% were male and 19% female. Respondents ranged in age from 18 to 75-plus, however, the majority were aged 35 to 54 (44%), followed by those aged 55 to 74 (38%). Responses from both 18- to 34-year-olds (13%) and 75-year-old and older (5%) rounded out participation from the youngest and oldest age groups.

When asked how their current vehicle was purchased:

- 35% responded, “new.”
- 54% responded, “used.”
- 9% responded, “CPO.”
- 2% of respondents claimed to not own a vehicle.

Of all respondents, 59% stated they were actively looking to buy a new or used vehicle.

### CPO Familiarity

Judging by the record numbers of CPO units sold over each of the past several years, consumer awareness of CPO programs has clearly improved. Even so, survey results indicate there is still a large percentage of consumers who know little about CPO programs.



While 39% of male respondents felt moderately to extremely familiar with manufacturer CPO programs, and 23% reported being somewhat familiar, over a third indicated they were only slightly, or not at all, familiar. Women were much less knowledgeable, with nearly 60% expressing little to no familiarity with the purchase option. Fewer than a quarter of female respondents felt they were moderately or extremely familiar with CPO programs.

Across age groups, awareness was lowest for 18 to 34 year olds. About 50% of these respondents stated they were either slightly, or not at all, familiar with CPO programs. By comparison, 40% to 44% of respondents from other age groups reported similarly low familiarity.

### CPO Consideration

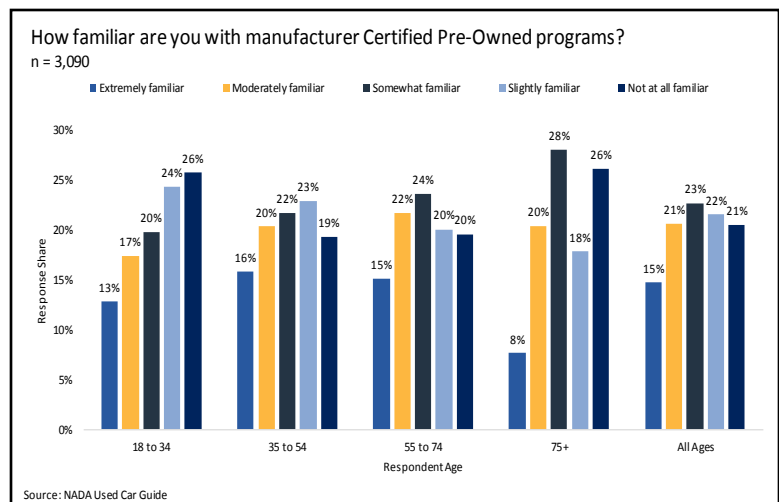
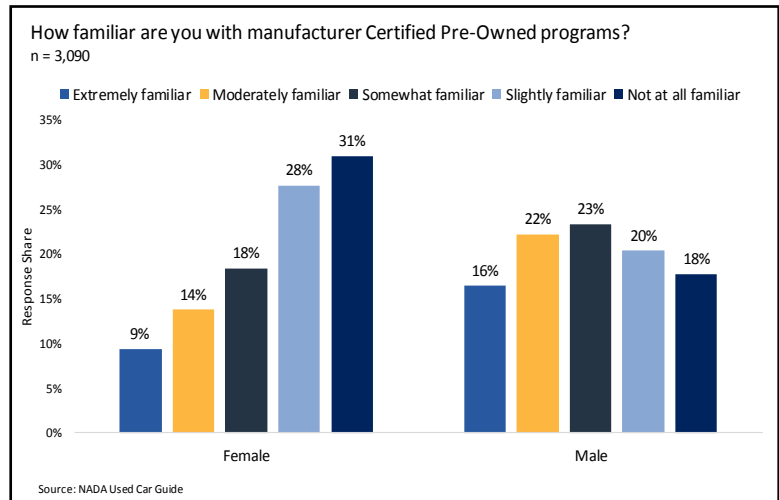
Two different questions were asked related to future CPO purchase consideration.

The first question, “What type of vehicle will you consider buying in the future?” was asked to gain a sense of where CPO consideration stands relative to new or non-certified used vehicles. The second question, “How likely are you to consider purchasing a Certified Pre-Owned vehicle in the future?” was asked to gauge the strength of consideration overall.

Regarding how CPO consideration compared to other sale types:

- 8% of respondents declared they would only consider buying CPO in the future.
- 17% stated they would strictly shop for new vehicles.
- 44% answered they would strictly buy used vehicles.

While the number of CPO-only shoppers was small, more than a quarter of respondents (27%) stated their willingness to consider CPO alongside either a new or used vehicle. Results were generally similar across age groups. Less respondents indicated they would seek out only new or CPO vehicles. The majority stated they would consider only a used vehicle, or a combination of new, used and CPO.





With 36% of respondents selecting all vehicle types, the 18- to 34-year-old age bracket exhibited the greatest willingness to cross-shop all vehicle types. Respondent openness to cross-shopping steadily declined as age increased.

When asked the second question, “How likely are you to consider purchasing a Certified Pre-Owned vehicle in the future?” 52% of 18- to 34-year-old respondents stated they were neutral in their commitment to a future CPO purchase. While the outcome was similar to what 35- to 54-year-olds shared, a larger percentage of younger participants (29% versus 26%) reported they were either, “likely” or, “extremely likely” to consider purchasing a CPO vehicle in the future. Future CPO purchase likelihood worsened as age ranges increased.

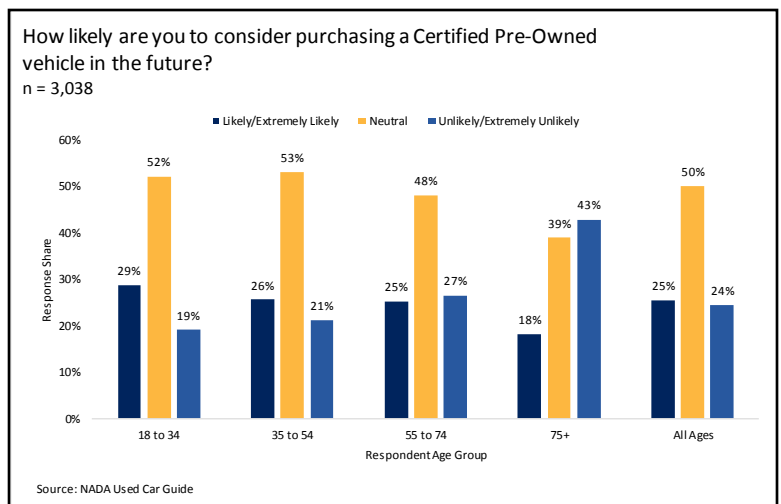
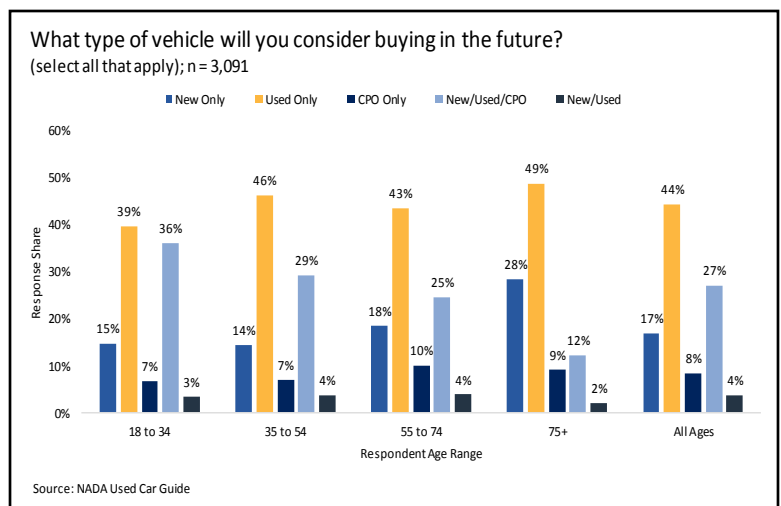
### CPO Premiums

Consumers were also asked to select a dollar amount they would be willing to pay for a CPO vehicle above and beyond a non-CPO used vehicle. The question was prefaced with a series of common CPO program benefits — comprehensive inspection and reconditioning requirements, an extended bumper-to-bumper warranty, etc. — to help respondents assign value.

Taken as a collective, the majority of respondents (39%) were willing to pay up to \$1,000 more for a CPO vehicle versus a non-certified used vehicle. However, a sizable 31% stated they weren’t willing to pay any premium for a CPO vehicle. The remaining 31% of responses were spread between \$1,000 – \$2,000 to more than \$4,000.

As might be expected, CPO premium results were much different when the data is grouped by the likelihood of a future CPO purchase. Of those stating they were, “likely” or, “extremely likely” to consider purchasing a CPO vehicle, 44% said they would pay up to \$1,000 more versus a non-certified vehicle. Just 11% said they would pay nothing. In addition, 22% stated they would pay \$1,000 to \$2,000.

Although the sample size is somewhat small (n=181), 36% of luxury vehicle consumers said they would pay a premium of up to \$1,000, while 32% would pay \$1,000 to \$2,000. Just 8% of self-proclaimed luxury buyers wouldn’t pay any premium. Given that NADA Used Car Guide mainstream and luxury brand CPO premiums currently average \$1,190



and \$2,160, respectively, consumer feedback among those willing to buy a CPO vehicle is generally in line with where premiums are actually transacting.

Of those claiming neutral intent toward a CPO purchase, the vast majority (44%) once again were willing to spend up to \$1,000. In contrast, a sizable 28% weren't willing to pay anything above and beyond the cost of a typical used vehicle. Not surprisingly, premiums were much lower for individuals claiming they were either unlikely or extremely unlikely to consider a future CPO purchase, with nearly 60% stating they would pay nothing.

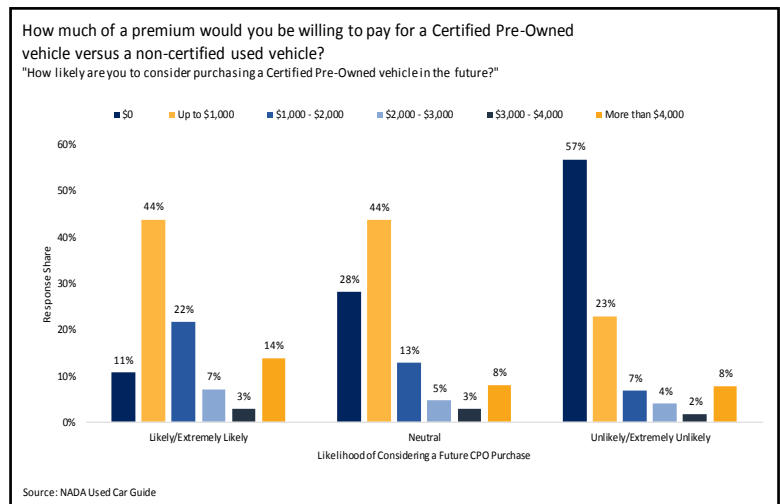
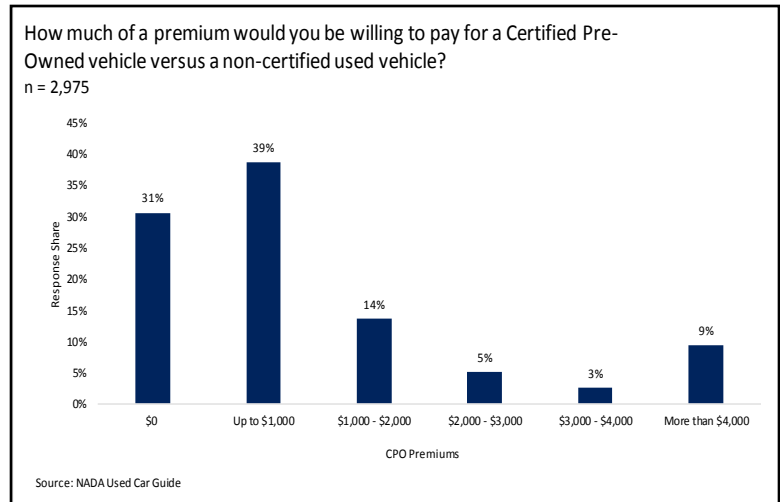
It should be noted that premium results based on purchase likelihood were generally similar when viewed by age, gender and level of CPO familiarity.

## CONCLUSION

When it comes to certified pre-owned programs, consumers and dealers alike are reaping significant benefits of buying and selling used vehicles through this purchase funnel compared to standard used sales.

For consumers, the peace of mind knowing that only vehicles in the best condition qualify — along with a rigorous multi-point inspection and reconditioning process, extended warranty protection, roadside assistance, as well as low interest financing — can make CPO units more appealing than their non-certified versions. For dealers, CPO vehicles are more easily marketed as relatively low-risk units. This product characteristic allows for higher prices than non-certified versions.

While manufacturers and dealers have done a good job growing CPO sales in recent years, consumer awareness has remained one of the biggest hindrances to significantly improved sales. The expected rise in off-lease supply — a major conduit of CPO stock — over the next several years should be especially important for improved CPO program awareness. J.D. Power forecasts off-lease supply to be over 64% higher in 2018 than it was in 2015. The unprecedented number of off-lease vehicles scheduled to hit the market means automakers will have to rely even more on CPO programs to help preserve used vehicle values.



The influx of used vehicle supply presents franchise dealers the opportunity to take greater advantage of revenue streams associated with CPO sales. As the results from the survey conducted on [NADAguides.com](http://NADAguides.com) indicate, maximum success can only be achieved if automakers and dealers improve consumer awareness on the benefits of Certified Pre-Owned vehicle ownership.

# AT NADA USED CAR GUIDE

## What's New

The new NADA Values Online introduces New Vehicle Values, a range of values that provide new vehicle pricing guidance based on actual market transactions and market influencers. It also includes inventory valuation, vehicle valuation trends and a custom reporting tool to help you see vehicle values from every angle.

With NADA Values Online, you have the data and insight you need to make better business decisions and see better outcomes.

**See how we can help your business >> Go to [nada.com/valuesonline](http://nada.com/valuesonline).**

## On the Road

Jonathan Banks will share NADA Used Car Guide's latest research on used value pricing at the annual Automotive Resource Network Conference in Atlanta, which runs August 2 – 3.

Learn from Jonathan Banks and Larry Dixon as they speak and present at the National Remarketing Conference (Used Car Week) in Las Vegas, November 14 – 18.

Say, "Hi" to Mike Stanton at the 2016 National Auto Auction Association conference in Las Vegas, November 16 – 18.

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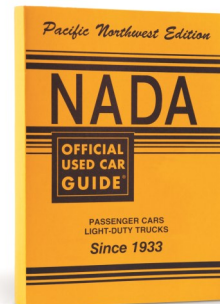
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**Financial Industry,  
Accounting, Legal,  
OEM Captive**  
Steve Stafford  
800.248.6232 x7275  
[Steve.Stafford@nada.com](mailto:Steve.Stafford@nada.com)

**Director, Sales  
and Customer Service**  
Dan Ruddy  
800.248.6232 x4707  
[Dan.Ruddy@nada.com](mailto:Dan.Ruddy@nada.com)

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Doug Ott  
800.248.6232 x4710  
[Doug.Ott@nada.com](mailto:Doug.Ott@nada.com)

**Director, Business  
Development**  
James Gibson  
800.248.6232 x7136  
[James.Gibson@nada.com](mailto:James.Gibson@nada.com)



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# NADA USED CAR GUIDE CONSULTING SERVICES

NADA Used Car Guide’s market intelligence team leverages a database of nearly 200 million automotive transactions and more than 100 economic and automotive market-related series to describe the factors driving current trends to help industry stakeholders make more informed decisions. Analyzing data at both wholesale and retail levels, the team continuously provides content that is both useful and usable to the automotive industry, financial institutions, businesses and consumers.

Complemented by NADA Used Car Guide’s analytics team, which maintains and advances its internal forecasting models and develops customized forecasting solutions for automotive clients, the market intelligence team is responsible for publishing white papers, special reports and the Used Car & Truck Blog. Throughout every piece of content, the team strives to go beyond what is happening in the automotive industry to confidently answer why it is happening and how it will impact the market in the future.

**VP, Vehicle Analysis & Analytics**

Jonathan Banks  
800.248.6232 x4709  
[Jonathan.Banks@nada.com](mailto:Jonathan.Banks@nada.com)

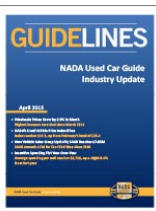
**Senior Manager, Market Intelligence**

Larry Dixon  
800.248.6232 x4713  
[Larry.Dixon@nada.com](mailto:Larry.Dixon@nada.com)

**Senior Analyst, Automotive**

David Paris  
800.248.6232 x7044  
[David.Paris@nada.com](mailto:David.Paris@nada.com)

## ADDITIONAL RESOURCES



### Guidelines

Updated monthly with a robust data set from various industry sources and NADA Used Car Guide’s proprietary analysis, *Guidelines* provides the insight needed to make decisions in today’s market.



### White Papers

NADA Used Car Guide’s white papers and special reports aim to inform industry stakeholders on current and expected used vehicle price movement to better maximize today’s opportunities and manage tomorrow’s risk.



### Perspective

Leveraging data from various industry sources and NADA Used Car Guide’s analysts, *Perspective* takes a deep dive into a range of industry trends to determine why they are happening and what to expect in the future.



### Used Car & Truck Blog

Written and managed by the Market Intelligence team, the Used Car & Truck Blog analyzes market data, lends insight into industry trends and highlights relevant events.

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