JEFF SMITH

The

KPI

Book

Second Edition

“The ultimate guide to understanding the Key Performance Indicators of your business”
Companion books in this series, written by Jeff Smith

Management Accounts Made Easy
*Written to be the perfect partner for The KPI Book*

How To Make More Profit With Your Service Department
*“The ultimate guide to understanding and improving your operational efficiencies”*

All Jeff Smith books are available to order directly from www.AskInsight.com
Coming in 2017… 

JEFF SMITH

Sales Process

“The ultimate guide to understanding how to increase sales and make more profit.”
What happens if we buy Jeff Smith's books for all our managers and they leave us?

What happens if we don't and they stay?
Dedicated to my three girls.
Sharon, Sophie and Lara

I love you more than anything.
(and you can’t beat that!)
(and you can’t say the same!)
(and you can’t say snap!)
(and I’ve written it in 5 books!)

...and to Max, you’ve wheedled your way in.
About The Author

Jeff Smith is the #1 Best-Selling Author, Business Strategist and Motivational Speaker who's made several programmes for Sky Television. He’s particularly well known for his ability to explain and convey complex information into jargon-busting, plain English that everyone understands.

His client list reads like a "who's who" of global success and includes nothing less than Royalty and a string of Fortune 100 companies. At the end of 2011 with book sales in excess of 50,000 copies he became regarded as one of the very best business improvement strategists in the world.

As a Motivational Speaker, Jeff speaks at conferences all over the world sharing the 7 big secrets of the world’s top achievers, focussing on how they use the most important Key Performance Indicators so you can discover how to make more profit and keep it.

If you would like to engage Jeff as a keynote speaker for your conference, or for a special training programme, you can contact him using the following details:

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A NOTE FROM THE AUTHOR

During my privileged and extraordinary journey within our wonderful industry, I’ve worked alongside the immense wealth of Royalty, the captains of industry in many fortune 100 companies, during which time I’ve come to the conclusion that key performance indicators are not mathematical formulae, they’re a philosophy with a meaning that goes far beyond just numbers.

Key performance indicators transcend race, colour and religion, they have no interest in geography, rank or opinion, they’re neutral, they’re the single thread that runs through the bellies of us all and unites us in business in a way that cannot be achieved by any other means.

They have the power of bypassing the doubters, the naysayers and the pessimists. They remain resolute, steadfast and sure, patiently lying in wait for those people who wish to take advantage of them.

You can simplify them or you can complicate them; you can agree with them or you can disagree with them; you can embrace them or you can turn away from them; just about the only thing you cannot do with them is to deny their existence.

They are the common denominators between our aspirations and our achievements, our hopes and our dreams, our budgets and our results. They are the roadmaps to success and the lenses through which we view and assess our business performance.

The people who use key performance indicators for the right reasons question everything related to operational
performance in the workplace. These are the people who come up with creative new ideas, devise new paradigms and often become the paradigm shifters themselves.

These people are the pioneers who push the boundaries of our industry forwards by challenging the norm to discover new ways of conducting and measuring business as our environment changes around us.

As time goes by these new methods and measures prove their worth, they’re tentatively accepted by others and then become redefined as industry Best Practice; and still the paradigm shifters continue to push on ahead.

In the beginning, some may see these people as stupid and crazy, whilst others see the passion within them. Revere the paradigm shifters because it’s the people who are stupid and crazy enough to think they can change our industry are the ones who do.
“Understanding the operational structure as well as the financial structure of your business is inseparable from your ability to influence its profitability”

- Jeff Smith
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INTRODUCTION

The only constant is change; in global terms, more change has taken place in the past 30 years than in the whole history of mankind put together. That itself is incredible, but from this point forward the pace of change is set to accelerate at an even faster rate and it’s our ability to cope with these changes that will make the difference between success and failure.

Most people hate change, yet it is the only thing that brings progress. We all have to cope with change and for most of us this can mean greater competition on both sales and profitability whilst our customers’ expectations continue to rise.

The challenge of change is to ensure that you take the right action at the right time to make the most of the opportunities that are available to you. New opportunities can mean new ways of working, which might mean that you need to think differently about your business in certain areas and try new ideas without discrediting them before you have any experience of the outcome.

The days have long since gone where you could simply increase your prices to increase your profitability. Nowadays, if you want to achieve better results in your business you are really saying that you want achieve different results in your business and this means changing the way you work in some areas. The amount of change you embrace is directly proportional to the different results you desire. Looking to the past and what you used to do will not always give you the answers you need for the road ahead; you can’t drive your car looking through the rear view mirror.
It’s important to understand the past, but it’s more important to be focussed on the future and sometimes you will need to walk new paths and lay new roads to arrive at your desired destinations.

But none of these things are easy to achieve in businesses that don’t like change. However, survival in business demands change, we cannot escape it and it’s forced upon us. New paradigms continue to shape our world of understanding, global recessions serve to cull the weak and those businesses that refused to change in the past no longer exist.

Being a manager and coping with change in the business environment is not always about chasing numbers and improving profitability, most of the time it’s about understanding people. If you and your team believe that change can add value to your business, your salaries and the desired change is a worthy cause to work for, most of the hard work has already been achieved. The implementation of new ideas is the easy part, but changing the hearts and minds of people is a little more difficult.

Whilst this book is about understanding numbers, it shouldn’t be forgotten that it’s people who are at the forefront of everything we desire. If we take the time to step back once in a while to understand our people and realise that we all have hearts, feelings and families, then the meeting of minds and a joint sense of purpose in life will be much easier and more enjoyable to achieve. It’s a wonderful feeling when people are working together in pursuit of a common goal; team work makes the dream work. Key performance indicators are merely the tools which provide the light in the areas of darkness.
How To Use This Book

To understand the structure and aims of this second edition, you first need a little background information of how it came to be, so let’s get started.

The first edition of The KPI Book was published on Friday 16 April 2001. When the first consignment of 1,000 books arrived, I opened the boxes and thought "What on Earth am I going to do with all these books!" I could not possibly have conceived the incredible journey in life that was about to unfold in front me.

Since that time, the book has become the automotive industry standard across the world and as a result I've been privileged enough to work with many different automotive businesses who provide cars, bikes, trucks and vans. Volume sales have ranged from the small businesses who sell less than 20 vehicles per year to the largest dealerships in the world who sell more than 5,000 vehicles per month and everything else in between; not to mention most of the manufacturers themselves.

The gruelling travel schedules have meant I've been flying to different countries every week, travelling through Europe, USA, The Middle East, Latin America Scandinavia, Asia and beyond. It's been very tough, but always very rewarding because it’s these experiences that have given me the knowledge to write this book from a truly global perspective.

This book contains pages of numeric examples for explaining the methodology behind key performance indicators and how to calculate them. The whole book is based upon a case study so that the examples given are
all real and relative to each other. This is to say that, if you wish, you can track performance right through Sales, Service, Parts and Bodyshop all the way through to the Balance Sheet.

Creating a case study to use for the examples in the book was crucial for establishing the proof required to standardise the global benchmarks and baselines. Nothing is random, nothing is based on opinion, nothing is left to chance; everything is based on hard facts and evidence.

**Understanding Benchmarks and Baselines**
The term benchmark is used when your performance is to be restricted between an upper limit and lower limit. Therefore performance benchmarks will always consist of two numbers; the upper limit and the lower limit. For example, the benchmarks for Utilisation are 85% to 95% which means that performance in this area should ideally be between these two limits. Benchmarks are therefore only useful to restrict thinking rather than to set an objective for things such as profitability. This is because when people reach a benchmark they usually stop and think, “That’s it, I’ve made it”.

Can performance be higher or lower than the benchmarks? Yes it can, but here’s the important thing…

> "Do not change the Benchmarks or Baselines to suit your own performance"

One of the main reasons for confusion with benchmarks and baselines is that historically, people have changed the
numbers to suit their own marketplace thinking that this is the way to go. However, as a result of this, we have different benchmarks all over the world and the key performance indicators lose their power.

The key to success with benchmarks is to compare your own performance with the standardised global benchmarks in this book and if there is a gap between your performance and the benchmarks, your task is to understand why the gap exists.

"It is not your task to achieve all the benchmarks and baselines. Your task is to understand your own performance within the context of your marketplace and your resources."

Benchmarks and baselines are not targets to be achieved; the numbers exist so that you have reference points for particular areas of performance within your business. If you change the benchmarks and baselines you no longer have any valid industry reference points. This means you can only compare your current performance against your own previous performance. Whilst it is useful and important to measure your own business trends, you still need the global perspective to provide you with a reference point so you can ask the right questions when assessing your performance.

It is the understanding of why there is a gap between your own performance and the global benchmarks that reveals the most power. If you change the benchmarks to suit your own performance, you lose the questions you
would have raised and therefore you will not understand why your performance is different to other regions around the world. Understanding the difference is the thing that makes the difference.

**Understanding Baselines**
The term baseline is used when you want to express a starting point for a given area of performance; this is a minimum expectation.

A baseline suggests that you should reach a given level of performance as an absolute minimum and you should continue to develop the area even further. On the contrary, a benchmark suggests that you should reach a given level of performance and maintain it.

Baselines are particularly useful when setting objectives in all levels of profitability because they do not have the limiting factor of setting an upper limit at which many people may stop any further development.

Care should be taken when measuring performance against both benchmarks and baselines because people have a tendency to aspire to what is expected of them, which may not necessarily be the same as achieving the optimum results from the resources available.

"The greatest danger for most of us lies not in setting our aim too high and falling short; but in setting our aim too low and achieving the mark."

- Michelangelo
Do all KPI have benchmarks or baselines?

No, this is not the case. There are many key performance indicators within the automotive industry and not all of them are created for the same reasons. If you can imagine going back in time to a place where the first key performance indicators were discovered, they were probably created by dealers and isolated to operational performance. In the case of understanding operational performance in the workplace, then the answer would be yes, each of these types of key performance indicators will have benchmarks or baselines. However, when we move forward in time and become more sophisticated, we created the desire to compare performance across regions and also across the world and so we saw the birth of the composite reports; a collection of dealer information which is then averaged across the group.

Composite reports are wonderful tools for understanding trends and in order to create a meaningful composite report, other new key performance indicators had to be created so that we can compare large companies with smaller companies. These types of key performance indicators will not have benchmarks and baselines because they become distorted to a large degree by the sample size of the group and not necessarily by operational performance in the work place in a single business. The sample size of a composite report can change results significantly and the peaks and troughs can be levelled out compared to an individual business.

The graph in figure 1, on the next page illustrates how a single business performance can compare with a composite average because a composite report with a large sample size can bring the peaks and troughs closer together and therefore level out performance. On the
other hand, a single business performance might be much more erratic and fluctuate beyond the composite averages due to its market conditions and the resources available.

**figure 1:**

![Graph showing single business performance against composite average.]

However, additional and useful information has been created and included within composite reports for budgeting tools for manufacturers, insurance companies and work providers. Unfortunately, some managers have misinterpreted these key performance indicators to be related to operational performance in the workplace.

A few of the more common KPI that fit into this criteria have been included within this book, but not all of them because the main focus of the book is on understanding and delivering operational performance in the workplace. Where these additional composite average key performance indicators have been included, no benchmarks or baselines will be given and instead the instruction will read with the following statement:

**Purpose:** Budgeting and Composite Analysis
This statement does not mean the composite average key performance indicators in question are worthless or useless; on the contrary, they are useful for the purposes for which they are intended. It does mean however that you should take care in the interpretation of these key performance indicators and not misinterpret them for other operational uses.

One such example is Hours Sold per Technician. You may use this KPI for budgeting purposes, but you must understand that Technicians do not sell hours; that’s the job of the Service Advisor or the Estimator so this KPI has no place on a day-to-day operational level.

The key to success with key performance indicators is to clearly separate cause and effect and if you want to make a difference in operational performance, you need to understand the effects and correctly identify the causes.

**Understanding Cause And Effect**

Actions are causes and results are effects. Think about a learner driver for a moment. Imagine a car is stationary at a junction in the road ready to turn right. The learner driver lets the clutch out too quickly and the car lurches forward faster than anticipated. The learner driver panics and grapples frantically with the steering wheel turning it quickly to gain control of the car.

The learner driver is dealing with the effects of their actions, not the causes. The cause of the car lurching forward is poor clutch control, but the learner driver tried to correct the problem by fighting the steering wheel. It doesn’t matter how adept the driver becomes with the steering wheel, the problem will always exist as long as the driver has poor clutch control.
The cause of the car lurching forward is poor clutch control and the effects are dealt with at the steering wheel. And so it is with the analysis of key performance indicators. Managers are so busy becoming adept with the steering wheel that they fail to gain control of the clutch.

Cause and effect should be equally recognised in business analysis if corrective solutions are to be applied. If the results in the company are less than satisfactory then different actions are required to generate different results. One clinical definition of insanity is to keep on doing the same things and to expect different results. If you want to change the effects in your business, you must change the causes. It’s not possible to change effects, it’s only possible to change causes; the same effects will always be evident until the causes are changed.

"All key performance indicators are effects. It’s your job to correctly identify the causes”

Becoming more adept at dealing with effects is counterproductive, energy sapping and pointless. In addition, simply throwing money at problems is treating the symptoms, not the disease and the problems are merely disguised for a little while until they return with a vengeance to ask for even more money at a later point in time.

When you want to improve operational performance in the workplace, you’ll continue fighting the effects, until you correctly identify and rectify the causes.
Defining purpose, goals and objectives
The Internet and cost effective travel has made planet Earth a global village. The gates of cross-border trading are wide open in most countries and we are all keen to know what other businesses are able to achieve in different areas of the automotive industry.

To have the ability to view each other’s performance is indeed a worthy goal, but we must all use a common language and understand the benefits and limitations in performance for these comparisons to make any kind of sense so we can exchange Best Practice initiatives.

My main aims in writing this book cover a multitude of areas. The first is to create a common language so that everyone can work together on a global scale and to understand the true meaning of each key performance indicator in a clear and simple way, without confusion.

Another aim is to introduce a brand new suite of key performance indicators into the Sales and Parts departments based on Operational Investment. These new key performance indicators are much more intelligent than the traditional measures such as Stock Turn because they assess how well managers utilise the funds entrusted to them for stock, the funding of that stock as well as credit control.

I created these new key performance indicators out necessity and stored them in my armoury of consultancy and training tools. Over the years, they’ve proven themselves to be invaluable and I now have the opportunity to share them here with you. They are a new set of paradigms so prepare your mind and get ready to challenge your current thinking.
There are also other brand new key performance indicators called Absorption Shortfall, Resorption and Sales Retention Index within the business section. These KPI are used for achieving strategic synergy between the Sales and Aftersales departments within a franchised dealership and illustrate how the Sales and Aftersales management teams have to work together to deliver the whole dealership results.

In addition to introducing these new key performance indicators, I also have a very personal goal. It is my greatest desire to bring people together across the world in the automotive industry and to achieve this, we need to standardise the benchmarks and baselines on a global scale.

This objective is of particular importance to me because it’s only when we have achieved this standardisation that we, as an industry, can have an in depth understanding of each other’s business performance on a truly global scale. Only time will tell if my efforts in writing this book are worthy of such mighty objectives.
Please note that this is a sample only and 99% of the content has been removed.
Understanding The Sales Departments: New, Used & Trade

“People often say perception is reality, but when it comes to management, performance is reality”

- Jeff Smith
% Value of Stock Over 90 days

Value of Stock Over 90 days ÷ Stock Value (x 100)

Baseline: < 10% of Stock Value

This KPI takes the total value of your new or used vehicle stock, and then states the collective value of the vehicles that are over 90 days old as a percentage of the total. In other words, if you have £3,692,997 invested in vehicle stock, how much of this money is invested in vehicles that have been in stock for more than 90 days?

Example:
A) Value of Stock Over 90 Days = £174,859
B) Value of Total Stock = £2,019,154
C) % of Funds Over 90 days = 8.66% (A ÷ B x100)

This KPI very wisely moves away from used vehicle units and measures the money that is invested within them.

The example above illustrates that 8.66% of the money that is invested in vehicle stock is currently invested in vehicles that have been in stock for more than 90 days. What the KPI does not tell you is how much longer than 90 days the investment has been there.

This is a very useful trend to assess because it measures the ability to manage the money that is invested in vehicle stock as opposed to the units themselves.

It removes the emotion that is often attached to those vehicles that someone will buy “one day”, and focuses your mind on the real issue at stake: Cash.
Adopted Stock

Fully Paid New Vehicle Stock

Baseline: Europe and USA = 0

In Europe, most new vehicle stock is supplied to a dealer from a franchise manufacturer on a consignment basis. This means that when new vehicles are delivered to the dealer, the dealer usually pays the interest charges or stocking charges as they are more commonly known.

After a defined period (typically 180 days) the new vehicles have to be adopted by the dealer, or in other words, the dealer must pay for the vehicles in full.

Before reaching the point of adoption, when a dealer sells a vehicle, the consignment agreement stipulates that the vehicle must be paid for at the point of registration. Therefore new vehicle stock is paid in full in one of two scenarios.

1) When the vehicles are registered  
2) When they reach the end of the consignment period

When vehicles reach the end of their consignment period they become Adopted Stock. The worst scenario that can happen is to be adopting vehicles because it absorbs huge amounts of money, which in turn prevents activity in other areas of your business due to cashflow.

In other regions around the world, consignment stock is not available and new vehicles are funded at source by the dealer. In these instances the dealer requires more cash of course, but is compensated with higher margins.
Advertising Cost per Unit Sold

£ Spent on Advertising ÷ Units Sold

Purpose: Budgeting and Composite Analysis

This KPI establishes the average amount of money that has been spent per unit sold. Beware! This is definitely \textbf{not} a measurement of your advertising effectiveness.

Example:
A) Money Spent on Advertising = £169,000
B) Units Sold = 960
C) £ Advertising per Unit Sold = £176.04 \((A ÷ B)\)

Firstly, the units sold should relate only to retail units and ideally, you should have a separate KPI for new and used vehicles.

This KPI is useful for ascertaining your advertising budget for retail sales, based on your sales objectives and it’s sometimes imposed by franchise standards by applying a percentage of the sales value. However, it should not be used to judge advertising effectiveness because that’s something different altogether.

If you wish to measure your advertising effectiveness, you would better using the advertising spend and dividing it by the number enquiries generated. The advertising might be very effective and generate many prospects, but if the sales process is weak, or product availability if poor, you may not convert those enquiries into sales and it would be quite wrong to blame the advertising for the lack of conversion.
Average Selling Price

Sales Value of Units Sold ÷ Number of Units Sold

Purpose: Budgeting and Composite Analysis

This KPI applies to new and used vehicles separately and provides you with your average selling price of the vehicles that you have sold.

Example:
A) Invoice value of vehicles sold = £20,409,600
B) Number of units sold = 960
C) Average Selling Price = £21,260 (A ÷ B)

This statistic is usually provided for you on your franchise manufacturer’s composite reports and shows the average selling price for new and used vehicles separately as opposed to being merged.

It is useful for establishing your funding requirements in stock when you are putting together your budgets, business plans and strategy plans such as model mix.

It is also useful in the assessment of your stock profiling exercises for used vehicles whilst your figures for the new vehicles will be heavily influenced by your fleet sales activity and your customer profile.

It is of course best to create this figure separately for New Retail, Fleet, Used Retail and Used Trade vehicles so you can more accurately assess the trends in each sectors. Once attained, you can also use this to identify the impact upon cash flow when matched with the seasonality of the sales volumes.
Circulation of Operational Investment (New)

Annualised New Vehicle Turnover ÷ Operational Investment of New Vehicles

Baseline: > 8

This KPI very cleverly asks how many times the capital investment at an operational level in new vehicles is being used in 1 year to generate the turnover. The higher the number the better because it demonstrates the Sales Manager’s ability to optimise the funds available.

Example:
A) New Vehicle Stock Value = £2,373,209
B) New Vehicle Debtors = £170,080
C) New Vehicle Creditors = £529,734
D) New Vehicle Turnover = £20,409,600
E) Operational Investment = £2,013,555 (A + B - C)
F) New Vehicle COOI = 10.14 (D ÷ E)

* See Operational Investment, New Vehicles on page 65.

The results here are influenced by Sales Volume, stock control and credit control so that the Sales Manager is responsible for all funds tied up and utilised within the generation of new vehicles. It’s all too easy to get excited by high sales volumes but money can easily get tied up in funding debtors for New Vehicles for Fleet Customers and poor control with finance companies. The smart Sales Manager focuses on how the stock is funded and maximises the creditors to reduce borrowings. This is especially useful in times of growth or with exceptional deals that need to be funded for longer periods because a downwards trend here is really bad news.
Stock Turn

Annualised Used Retail Unit Sales ÷ Used Unit Stock

Baseline: > 8 times per annum

Used vehicle Stock Turn tells you the number of times that you use your used vehicle stock in 1 year; the higher the number, the better.

Example:
A) Annualised used Retail vehicle sales = 1,462
B) Number of units in used stock = 152
C) Annual Stock Turn = 9.62 (A ÷ B)

This example illustrates the used vehicle stock being utilised 9.62 times per year; note that consignment stock should also be included and Trade Sales are excluded.

Quite simply, the faster you turn your used vehicle stock, the less money you need to invest. The baseline of 8 times per year is an urban myth and represents mere survival. You want to achieve closer to 10 times per year; the top achievers deliver 12 times per year or more.

Stock Turn has been the traditional KPI used to assess how well a Sales Manager uses the stock, but it falls short in quite a few places because it only counts units and makes no reference to the profits generated, the management of the investment, credit control or indeed the value of stock. To gain the complete picture, please also see Circulation of Operational Investment on page 35 and in conjunction with that Return on Operational Investment on page 74. These KPI look more closely from a business perspective.
Stock Turn Days *(Used Retail Vehicles)*

Units in Stock x 365 ÷ Annualised Retail Units Sold

Baseline: < 45 Days

This is also known as Days Supply or Days Stock Turn. The KPI questions how many days, on average, used vehicles remain in stock prior to being sold.

Example:
A) Used Vehicles in Stock = 152
B) Days in 1 year = 365
C) Used Retail Sales = 1,462
D) Stock Turn Days = 37.94 days \((A \times B ÷ C)\)

This example is illustrating that used vehicles remain in stock for an average period of 37.94 days prior to being sold. This figure is of course an average of the entire stock and of course some vehicles sell within the first 10 days or less and others may remain in stock for 60 days or more.

Evidence from the top achievers confirms that dealers with this KPI reporting lower than 40 days have significantly higher gross profit in used vehicles and lower expenses than those dealers who report 50 days stock turn or more.

The higher the figure, the worse the situation because it confirms that vehicles are remaining in stock for longer periods of time. Not only does profitability fall, but you will also be attracting overage stock, which brings with it a whole host of other undesirable problems. 45 days is tolerable, but 36 days or lower would be a good result.
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Jeff Smith’s Law Of The Service Department

“Assumptions are dangerous, they lead the naive in all directions. Uncover the evidence and discover the truth”

- Jeff Smith
Jeff Smith’s Law of The Service Department

Wouldn’t it be a wonderful world if all manufacturers, Dealer Principals, Accountants, Service Managers and Staff in every dealership in every country used the same words to describe the operational efficiencies of the Service Department? As we’re dealing with hundreds of thousands of people here, understandably, this is not the case and what we have to work with is a myriad of terms that essentially mean the same thing… or do they?

The meaning of the term Productivity can mean one thing to one person and yet something completely different to another, and something else again to another, yet the crazy thing is, they can all be correct. It can be so frustrating, especially when all of these people are insisting that they’re using the correct term and you’re the one who’s wrong.

In addition to the naming conventions being used in different ways, we also have inconsistent benchmarks and in some cases, they’re obviously plucked out of thin air because they make no sense at all. It comes as no surprise that we have so much confusion surrounding these three operational efficiencies, hence it’s so difficult to extract and share best practice.

To combat this wide-spread industry problem, this section has tackled the issue head on and cleared up all the controversy surrounding the benchmarks. Here you will see the truth revealed; not by opinion, but rather by evidence. All the folklore and myths that have been passed from one manager to another have been stripped away to lay bare the cold, hard facts of reality to eliminate all confusion.
The Construction and Methodology of Jeff Smith’s Law of the Service Department

**Stage 1:** The business model is based upon a simple equilateral triangle which is split into three sectors labelled Sector A, Sector B and Sector C.

*Figure 1:*

![Equilateral triangle with sectors labeled](image)

Although it may appear simple, it’s worth taking the time to memorise the exact layout of the triangle because you will need to recall this information at a later stage when the naming conventions for the Service Department operational efficiencies are introduced into each sector. And perhaps more importantly, you will need to understand how the benchmarks are created which is a direct result of the placement within each sector.
Stage 2: Here we can see the most important aspect of the business model because the sectors are not randomly paced within the triangle; there’s method. The arrows and the mathematical operators are displaying how the sectors are relating to each other with the examples below showing the results.

Figure 2:

Results from above:

\[ A \div B = C \]
\[ A \div C = B \]
\[ B \times C = A \]
Content removed – Sample only
Efficiency
(Models 2, 3 & 4, Sector C, pages 103, 104 and 105)

Hours Sold ÷ Hours Worked (x100)

Benchmarks: 110% to 125%

This KPI questions the relationship between the Technicians speed in completing jobs and the selling skills of the Service Advisor.

Example:
A) Hours Sold = 28,563.13
B) Hours Worked = 24,691.50
C) Efficiency = 115.68% \((A ÷ B \times 100)\)

Contrary to popular belief, this is not a measure of the Technician’s beating the manufacturers’ book times; instead it measures against the Hours Sold. To assess Technician speed, see Technical Efficiency on page 126.

The responsibility of the Hours Sold sits firmly with the Service Advisor. On some occasions they may not invoice the completed work, in which case it will stay in Work In Progress and not show in the Hours Sold. Other influencing factors are the inclusion or exclusion of diagnostic work, inaccurate invoicing and poor selling skills.

The danger here is that if Technicians speed up and complete their jobs in faster times, Efficiency will increase, but the workshop may run out of work and simply create Idle Time. Therefore this KPI must be analysed in the context of Jeff Smith’s Law of The Service Department to ensure the correct interpretation.
Labour Utilisation
(Model 6, Sector B, page 107)

Hours Worked ÷ Hours Attended (x100)

Benchmarks: 85% to 95%

This KPI asks how much of the Technicians Attended time is actually spent spanner-in-hand, head-under-bonnet, clocked onto a job card.

Example:
A) Hours Worked = 24,691.50
B) Hours Attended = 27,000
C) Labour Utilisation = 91.45%  (A ÷ B x 100)

This example shows that Technicians have attended 27,000 hours of which 91.45% of that time has been spent clocked onto jobs. In other words, 91.45% of the time available to work has been utilised. The remaining 2,308.50 hours, which is 8.55% of the hours attended that was not clocked onto jobs will be shown as Idle Time.

\[
\text{Labour Utilisation} = 91.45\% \\
\text{Idle Time} = 8.55\%
\]

It’s influenced by the speed at which the Technicians complete their jobs and the number of hours available to work. The danger here is that if Technicians slow down, Labour Utilisation will increase, so it must be analysed in the context of Jeff Smith’s Law of The Service Department to ensure the correct interpretation.
Understanding The Service Department

“To give real service, you must add three ingredients which cannot be bought or measured with profit: sincerity, passion and integrity.”

- Jeff Smith
Debtor Days

Service Debtors ÷ Service Daily Credit Turnover

Baseline: < 45 days

The Debtor Days KPI is a measurement of the credit activity within the Service Department. Its purpose is to inform you of the average number of days that your customers take to pay you.

Example:
A) Service Debtors = £102,129
B) Service Daily Credit Turnover* = £2,360.28
C) **Debtor Days** = 43.27 \( \frac{A}{B} \)

*Note:*
In order to calculate the Service Daily Credit Turnover, you will need to take the annualised Service Turnover which is sold on credit and divide that figure by 365 to arrive at a Service Daily Credit Turnover.

Example:* 
A) Annual Turnover On Credit = £861,500.53
B) Days in 1 year = 365
C) Service Daily Credit Turnover = £2,360.28 \( \frac{A}{B} \)

In the example provided above the average amount of debt is outstanding for a period of 43.27 days. In many cases, customer credit agreements are for 30 days and all too often these credit terms are not fully instigated and your money is outstanding for longer periods of time. The question is how much longer? A business can survive a long time without profit, but it cannot survive a single day without cash.
Department Contribution

Department Contribution ÷ Turnover (x100)

Baseline: > 35%

The Contribution of the Service Department is also called many other things such as, Department Profit, Operating Profit, Direct Profit and of course the bottom line.

Contribution is calculated by taking Gross Profit minus all Department Expenses. To make sense of this figure it is always expressed as a percentage of Turnover when used for trending as it’s the direction of travel that is of most interest to you.

Example:
A) Contribution = £1,842,607.25
B) Department Turnover = £4,786,114.08
C) Contribution % = 38.50%  \( \frac{A}{B} \times 100 \)

Keeping track of your Contribution % is best shown in the form of a simple graph that is updated monthly so that you can see the trends that are emerging.

However, this figure by itself will not help you much because you need to get behind the scenes and examine your Gross Profits and Expenses to understand the causes for both good and poor performance.
Department Expenses

Department Expenses ÷ Turnover (x100)

Baseline: Own Strategy

The Department Expenses of the Service Department are also known as Direct Expenses and refer to the total expenses incurred. They represent the sum total of the Variable Expenses and Semi-Fixed Expenses.

Typically, Department Expenses are shown as a monetary value and in order for you to capture meaningful trend analysis you will need to express them as a percentage of department Turnover.

Example:
A) Variable Expenses = £115,640.05
B) Semi-Fixed Expenses = £1,884,898.00
C) Department Expenses = £2,000,538.05 (A + B)
D) Department Turnover = £4,786,114.08
E) Department Expense % = 41.80% (C ÷ D x 100)

Keeping control of Department Expenses can be a difficult task unless you fully understand the difference between Variable Expenses and Semi-Fixed Expenses.

Variable Expenses are directly linked to sales volume and Semi-Fixed Expenses are not linked to sales volume therefore the actions that you need to take to maintain control is different in each area.

Simply looking here and not fully understanding the differences in expenses can be very misleading and therefore dangerous; take care with this one.
**Diverted Time**

**Hours Attended – Hours Worked**

**Benchmarks: 5% to 15% of the Hours Attended**

This term is also known as Unrecovered Time, Idle Time or Lost Time.

Diverted Time means that the Technicians have been attending the dealership and available to work, but they have not been clocked onto jobs. Typically this could be due to a lack of work available, time spent locating a vehicle, or waiting for parts and other such issues.

Example:

A) Hours Attended = 27,000  
B) Hours Worked = 24,691.50  
C) **Hours Diverted** = **2,308.50** (A - B)  
D) Average labour Cost = £22.50  
E) **Cost of Diverted Time** = **£51,941.25** (C x D)

The mathematical formula is simply Hours Attended minus Hours Worked and this is shown here as a number of hours and a monetary value, which can usually be found within the Variable Expenses of the Service Department.

There’s often a big misunderstanding here which is that this represents Technicians time that has not been sold; this is incorrect. The truth is that this is the Technicians time that has not been worked. Technicians don’t sell hours, they work hours, it’s the Service Advisor who sells the hours and that’s a completely different function, performed by different people at different times.
Lead Time

“I want my vehicle serviced, when can you fit it in?”

Baseline: 3 days or less

The Lead Time is the length of time a customer must wait before their vehicle can be seen by your Service Department.

A short Lead Time of two to three days is usually expected and generally accepted by a customer unless they have a serious problem that needs immediate attention.

A long Lead Time of seven to ten days is not generally understood nor accepted by customers and usually results in them taking their vehicles elsewhere; forever!

Factors that affect the length of Lead Time are the availability of Courtesy Cars, collection and delivery, workshop loading, customer retention, and Aftersales marketing. The length of Lead Time that your dealership has is a reflection of the work that is available to you and to be truthful, your ability to cope with its demands.

If your Lead Time is seven days or more on a consistent basis, then you should certainly examine the capacity of your workshop and you may consider taking on additional Technicians if you have the facilities available, or review your courtesy car procedures.

If your Lead Time is nonexistent on a continual basis, then your Aftersales marketing campaigns may need an extra boost to gain additional work.
Retail : Internal Ratio

Retail Hours Sold ÷ Internal Hours Sold

Baseline: >2.5:1

When you wish to grow a Service Department, you need to see real growth in the Retail Hours Sold, but simply having more Retail Hours Sold is not enough, you need to see growth against the Internal Hours Sold which means that Customer Retention is good and the department is not reliant upon the Sales Department.

Example:
A) Retail Hours Sold = 19,994.19
B) Internal Hours Sold = 5,712.63
C) Retail : Internal Ratio = 3.5:1 (A ÷ B)

One of the factors affecting this statistic is a rapid growth rate in vehicle sales, which in the short-term will shift the bias to internal work. However in the following months the balance should be redressed as these vehicles return for scheduled servicing. If those vehicles do not return, this ratio will show a downward trend.

If the underlying trend of this KPI is demonstrating a high dependence upon internal work, it could mean that your dealership is losing its retail customers, there are no efforts in place to grow the retail sector of your business, or there is little or no control for invoicing procedures between the Sales and Service Department.

This is a strong indicator of the Service Manager’s ability to grow the workshop without the reliance upon internal and warranty work.
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Interpreting Your Parts Department

“Profit Loves Speed”

- Jeff Smith
Average Buying Margin %

Retail Value – Net Invoice Value ÷ Retail Value (x100)

Baseline: Franchise Specific

This KPI informs you of the average profit margin that is applied to every purchase that you have made, or in other words, it’s the average amount of mark-up that you have available.

Example:
A) Retail price of purchases = £8,134,545
B) Cost of parts purchases = £5,541,157
C) Average buying margin = £2,593,388 (A – B)
D) Average Buying Margin % = 31.88% (C ÷ A x 100)

This example shows that for this particular accounting period, the parts purchases amounted to £5,541,157 and the retail price of those parts is listed at £8,134,545; the difference between them is your profit margin.

The average buying margin in this example is looking at the total parts purchases whereas the source of purchase may be different and may have different buying margins; for instance, Stock Order purchases. VOR purchases, purchases from other businesses and of course different product groups may also have different buying margins.

The calculation is an average of all purchases made in a given period, usually 1 month, but many reports will show you the Average Buying Margin across the different product lines and product groups. Typically, you can find your buying margins on the reports supplied to you by your franchise manufacturer.
Circulation of Operational Investment

Parts Turnover ÷ Operational Investment (x 100)

Baseline: > 8

This KPI very cleverly asks how many times the capital investment at an operational level in the Parts Department is being utilised in 1 year in order to generate the turnover. The higher the number the better because it demonstrates the Parts Manager’s ability to optimise the funds in use.

Example:
A) Parts Stock Value = £745,690
B) Parts Debtors = £229,384
C) Parts Creditors = £269,886
D) Parts Dept. Turnover = £7,486,728.73
E) Operational Investment = £705,188 (A + B - C)
F) Parts Department COOI = \(10.62\) (D ÷ E)

* See Parts Operational Investment on page 201

The results here are influenced by Sales Volume, stock control and credit control so that the Parts Manager is responsible for all funds tied up and utilised within the generation of parts turnover. It’s all too easy to get excited by high sales volumes but money can easily get tied up in funding Debtors for Trade Sales with poor credit control. The smart Parts Manager focuses on how the stock is funded and maximises the creditors to reduce borrowings. This is especially useful in times of growth or with exceptional Trade deals that need to be funded for longer periods. Beware, because a downwards trend here absorbs cash and destroys profitability.
Circulation of Stock

Parts Turnover ÷ Stock Value (x 100)

Baseline: > 8

This KPI is similar to Stock Turn and uses the same kind of thinking, but instead of using Sales at cost price, it uses sales at invoice value. It’s asking how much stock is required to generate the turnover.

Example:

A) Parts Turnover = £7,486,728.73
B) Parts Stock Value = £745,690
C) Circulation of Parts Stock = 10.04 (A ÷ B)

This KPI is a little wiser than Stock Turn as it takes the value of discount into consideration because the sales value is the invoice value, which is after discount. If Parts Sales business is growing, but with higher discounting, this KPI will reduce meaning that you’re using more stock to generate your sales.

In simplistic terms, the faster you circulate your stock, the less money you need to invest and the faster it is selling. Both of these facts mean that you will avoid overage stock and the losses associated with it. Of course the slower the circulation, the more money you need to invest and you will attract more overage stock.

However, whilst this KPI does take the value of stock into account, it doesn’t explore how that stock is funded, nor how the Parts Manager optimises the funds of the department. To get the complete picture, please see Circulation of Operational Investment on page 182.
Emergency Order %

Purchases on E.O. ÷ Total Purchases (x 100)

Baseline: Depends upon frequency of Stock Order

E.O. is an abbreviation for Emergency Order. E.O. sales occur when a vehicle is being repaired in the workshop and the parts that are required to repair it are not currently held within your parts stock so an Emergency Order is placed with the manufacturer.

Example:
A) Emergency Orders = £759,739
B) Total of parts purchases = £5,541,157
C) Emergency Order % = 13.71% (A ÷ B x 100)

In this instance, the required parts are ordered from your franchise manufacturer on an emergency basis and the parts are delivered much faster than they would otherwise be delivered on a stock order. But beware, they often carry a price penalty so you pay more for the privilege.

This KPI is captured on a monthly basis and this example is showing that 13.78% of the purchases in this particular period were ordered on an EO basis. The percentage of EO order is dependent upon the Parts Manager’s ability to select the right items for stock and it’s also dependent upon the frequency of the stock order.

A European business model should have no more than 10% E.O. purchases, whereas a business with a very slow supply chain and a monthly stock order could see the EO% up towards 30% in some instances.
Obsolete Stock

Baseline: < 1% of Turnover per month

Wouldn’t it be a wonderful world if you were able to sell every single part that you purchased? The truth of the matter is that you are unable to achieve this utopia in the real world and therefore you have to make decisions about how long you keep hold of stock before you admit to yourself that it’s just not going to sell.

Although the parts which are occupying your shelves right now do not have a “sell by date” printed on them, you already know that there is a limited amount of time for them to sell because new vehicles are being launched and demand for older parts diminishes. Once this time has expired, those old parts are said to be past their sell by date, or in other words, they become obsolete stock.

There are no hard and fast rules for writing off parts stock, but Best Practice in Europe and the US seems to be around 2 years. After the first year, 50% is written off and after the second year the remainder is written off and the parts are then discarded. The amount of write off should not be greater than 1% of your turnover each month. If it’s higher, then you have too much stock, or even worse, too much of the wrong stock.

In other regions such as The Middle East, Asia and Latin America, parts obsolescence is often not recognised (sometimes by the dealer and sometimes by government legislation) and parts stock continues to grow with obsolete parts remaining in stock at full price. This poor practice creates a higher taxation liability and dangerous distortions in the business on Cashflow and Gearing.
Return on Operational Investment

Parts Dept. Profit ÷ Operational Investment x 100

Baseline: > 96%

This KPI questions the whole department profit for 1 year being returned from the operational investment that’s been placed within the Parts Manager’s control.

Example:
A) Parts Stock Value = £745,690
B) Parts Debtors = £229,384
C) Parts Creditors = £269,886
D) Parts Department Profit = £1,207,063.41
E) Operational Investment = £705,188 (A + B - C)
F) ROOI = 171.17% (D ÷ E x 100)

This is the ultimate measure of the Parts Department because it questions how much profit is being made based upon how much you have invested within it.

This KPI is the best measure of a Parts Manager because it calls into question the control of profitability, expenses, stock levels, credit control and indeed how the stock is funded, including Imprest Stock.

When making strategic decisions within the Parts Department, it’s always wise to consider the impact that your decisions have upon this KPI. The top achievers in the industry achieve much more than double the baseline given here and it’s achieved by making decisions quickly, properly managing funds and operating without excess stock. A diminishing trend here is really bad news because it drains cashflow.
**True Parts Stock Turn (Version 1)**

**Annualised Stock Purchases ÷ Stock Value**

**Baseline: Dependent Upon frequency of Stock Order**

This KPI is valuable when you wish to know how many times the Parts Manager uses the funds invested in the parts stock; the higher the number the better.

Example:
A) Annualised Stock Order Purchases = £3,876,292  
B) Annualised VOR. Purchases = £759,739  
C) Annualised Other Purchases = £905,126  
D) Current Stock Value = £745,690  
E) **True Parts Stock Turn** = 5.20  \( \frac{A}{D} \)

Please note that VOR and Other Purchases are excluded from this equation because those orders are not intended for stock purposes. They come in and go out with immediate effect because they were required for a customer and were not in stock at the time of the order. Please compare the result here with the Total Stock Turn on page 214 and you will clearly see the difference.

You may need to calculate the True Parts Stock Turn yourself as this is seldom shown on Composite reports; many use the Total Stock Turn shown on page 214.

The baseline is wholly dependent upon the frequency of the Stock Order. A European and US business model typically has stock order terms of 3 days or less and has little requirement for stockholding; they should achieve a figure of at least 6 times, whereas a country with a very slow supply chain may slip down to 3 times per year.
**Bodyshop Efficiency**  
(Model 5, Sector A, page 240)

**Hours Sold ÷ Hours Attended (x100)**

**Benchmarks: 93.5% to 142.50%**

This KPI measures the abilities of the Bodyshop Manager, the Technicians and the Estimator to control everything because it illustrates the balance between Working Efficiency and Selling Efficiency.

Example:
A) Hours Sold = 27,636.80  
B) Hours Attended = 21,600  
C) **Bodyshop Efficiency** = 127.95% \( \frac{A}{B} \times 100 \)

Bodyshop Efficiency is about maximising the whole Bodyshop to ensure the following 5 areas are optimised:

1) Establish the optimum number of Hours Attended.  
2) When the Technicians are available to work, make sure they are working on jobs.  
3) When the Technicians are working on jobs, ensure that they complete the jobs quickly to save time.  
4) Here’s the key…In the time the Technicians have saved by working quickly, you must load additional jobs into the time saved or you will just be left with Idle Time.  
5) Ensure that the invoices are completed accurately and all of the work is sold to the customer.

High levels of Bodyshop Efficiency produce high levels of profit. The secret to success is to optimise Step 4 by loading the Bodyshop to ensure you have enough work to fill the gap created by the time saved.
Productive Efficiency
(Model 6, Sector C, page 241)

**Hours Sold ÷ Hours Worked (x100)**

**Benchmarks: 110% to 150%**

This KPI questions the relationship between the Technician's speed in completing jobs and the selling skills of the Estimator and the people at the front counter.

Example:
A) Hours Sold = 27,636.80
B) Hours Worked = 20,234.88
C) **Productive Efficiency** = 136.58% \((A ÷ B \times 100)\)

Contrary to what most people think, it is *not* a measure of the Technician's ability to beat the agreed job times. This is because the measure is against the Hours Sold and not the allocated job time; To assess Technician's speed, see Technical Efficiency on page 260.

The responsibility of the Hours Sold sits firmly with the Estimator. On some occasions the invoice may not be produced in the same time period in which the work is completed and the job will stay in Work In Progress and not show in the Hours Sold. Other influencing factors are estimating skills, inaccurate invoicing and selling skills.

The danger here is that if Technicians complete their jobs in faster times, Productive Efficiency will increase, but the Bodyshop may run out of work and simply create Idle Time. Therefore this KPI must be analysed in the context of Jeff Smith’s Law of The Bodyshop to ensure the correct interpretation.
Understanding The Bodyshop

“There are no secrets to success. It’s the result of hard work, preparation and above all, learning from your mistakes.”

- Jeff Smith
Cycle Time

First Notification Of Loss (FNOL) to Handover

Purpose: Budgeting and Composite Analysis

Cycle Time has been created by work providers to obtain an “average cycle time” which is ideal for their own cost control purposes and for these reasons it makes sense when they have such a large sample size of repairs.

However, from a Bodyshop Management perspective this can be completely misinterpreted because there’s no such thing as an average job, which means that Cycle Time can vary based upon the type and mix of jobs you receive rather than the time it takes to complete those jobs.

Another distortion here is that different work providers have different criteria for measuring the Cycle Time, which means that if you have multiple work providers, you may also have multiple versions of Cycle Time; here are three more variants of Cycle Time as an example:

1) FNOL to Invoice
2) Vehicle receipt to invoice
3) Vehicle receipt to vehicle handover

There are indeed many more versions and none of them are right or wrong. However, applying any form of Cycle Time on a day-to-day basis within a Bodyshop can be very misleading because the sample size of repairs is so much smaller than the sample size of the work provider. This means that you cannot accurately compare Cycle Times because the average times will be very different. Please also see Key-To-Key on page 281.
Estimate Conversion Ratio

Nº of Jobs from Estimates ÷ Nº of Estimates (x100)

Baseline: > 80%

This KPI assesses how many jobs you have gained from the estimates that you have given.

Example:
A) Nº of jobs from estimates = 1,404
B) Nº of estimates given = 1,654
C) Estimate Conversion Ratio = 0.85:1 (A ÷ B)

More often than not, this KPI is referred to as a ratio, but in terms of reporting format it is usually displayed as a percentage.

The measurement is exactly the same the only difference is that you multiply the result by 100 to convert the ratio into a percentage. It’s really a matter of your preference.

Example:
A) Nº of jobs from estimates = 1404
B) Nº of estimates given = 1,654
C) Estimate Conversion % = 84.89% (A ÷ B x 100)

In simplistic terms these examples show that for every estimate that you have provided, you have successfully converted 84.89% of them into jobs for your business.

There are 2 things to examine here, the accuracy and selling skills of the Estimator and the selling skills of the person doing any follow-up calls to question why you have not received the approval as yet.
Recovery Rate *(Overall)*

Total Labour Sales ÷ Total Hours Sold

Baseline: See Recovery Rate %

Your Bodyshop will have a published labour rate per hour, (Charge out Rate) but how often are you able to charge this amount to every customer on every job without giving a discount?

The Recovery Rate is asking how much revenue you have recovered per Hour Sold after any discount.

Example:
A) Retail Charge Out Rate = £65 per hour  
B) Hours Sold = 27,636.80  
C) Labour Sales without discount = £1,796,392 (A x B)  
D) Actual Labour Sales = £1,394,511.71  
E) **Recovery Rate** = £50.46 (D ÷ B)

This example shows the charge out rate is £65 per hour, but after discount, the amount recovered is £50.46 per hour. This means there’s an average discount of £14.54 being given on every hour sold. Apart from controlling the discount levels, there are two main issues here:

1) In which income stream is the discount being given? For this you need to calculate the Recovery Rates for each income stream you have such as Retail, Insurance, Internal and Warranty (and any other income stream) then the discount will become visible.
2) To compare your performance against other Bodyshops, you need to calculate the Recovery Rate % for each income stream.
Content removed – Sample only
Interpreting Your Business Information

“Turnover is vanity, profit is sanity, cash is reality.”

- unknown
Absorption *(Basic Version)*

Aftersales Direct Profit ÷ Business Overheads (x100)

**Baseline:** See Advanced Version on the next page

This basic version of Absorption asks if the combined Direct Profits from Aftersales have the ability to cover (absorb) the cost of the company overheads.

Example:
A) Direct Profit from Aftersales = £3,804,329  
B) Company Overheads = £4,590,595  
C) Overhead Absorption = 82.87% \( \frac{A}{B} \times 100 \)

Aftersales Direct Profit means the collective profits generated from all areas of the dealership with the exception of the Sales Department profit.

It doesn’t mean that Aftersales is more or less important than the Sales Department, it’s simply that Aftersales profitability is less volatile than the Sales Department profitability so it’s more stable for planning purposes in this scenario.

This example demonstrates that 82.87% of the company overheads are covered by Aftersales, which leaves the remaining 17.13% of the company overheads to be covered by the profits from the Sales Department.

This basic version only questions the company overheads, but if you need to assess company breakeven, you also have to consider what other expenses are evident apart from the company overheads; this is where the advanced version takes over on the next page.
Circulation of Investment (COI)

Annualised Company Turnover ÷ Investment

Baseline:
- **6 times per annum** (if property is on the balance sheet)
- **12 times per annum** (if property is not on the balance sheet)

This KPI is questioning how well, or to be more specific, how many times the management team is using the total investment within the company over the period of 1 year in order to generate its revenue.

Example:
A) Company Turnover = £62,914,213
B) Investment = £9,387,385
C) **COI = 6.70 times p/a** \((A ÷ B)\)

This example is showing that the management team has used the investment 6.70 times in the current 12 month period. Essentially, the higher the number the better because a higher number means that you need less investment in the company to enable it operate. In addition, the lower the Investment, the higher the Return On Investment. A low or diminishing trend is really bad news as most companies that go bust, do so because of poor performance in this area which leads directly to cash flow difficulties.

There are many factors that have an impact upon COI, but it’s important to realise that many of them are operational as opposed to financial and this is the main reason why Operational Investment and Circulation of Operational Investment has been created and added to the departmental KPI in this book.
**Current Ratio**

**Current Assets ÷ Current Liabilities**

**Benchmarks: 1.25:1 - 1.3:1**

This KPI establishes whether you have the correct level of Working Capital in your company to enable it to survive on a day-to-day basis to conduct the process of buying and selling your products and services.

Example:

A) **Current Assets** = £5,883,860  
B) **Current Liabilities** = £4,561,132  
C) **Current Ratio** = **1.29:1** \((A ÷ B)\)

This example is showing a Current Ratio of 1.29:1, which means that for every £1 of Current Liability you have £1.29 in Current Assets.

It's rather like the company's blood pressure test. If Current Ratio is less than 1.0:1, you’re technically insolvent which means you have no Working Capital and your business dies. However, if Current Ratio continues climbing up and over 1.3:1 that could mean you have too much Working Capital and it’s lying dormant and not working for you. Too much working Capital is like high blood pressure; it’s not a good thing.

The benchmarks for Current Ratio are generally higher in the automotive industry than in other industries because the nature of our business dictates that our stocks are always suffering the effects of depreciation and as an industry, we have the tendency to pay out money at a faster rate than we receive it.
Debtor Creditor Ratio

Debtors ÷ Creditors

Baseline: < 1:1

This KPI is questioning the amount of money your customers owe your business compared with the amount of money that your business owes your suppliers.

Example:
A) Debtors (Accounts Receivable) = £712,006
B) Creditors (Accounts Payable) = £1,027,228
C) Debtor Creditor Ratio = 0.69:1 (A ÷ B)

As you can see from the example above, on one hand you are loaning money to other companies (Debtors) and on the other hand you are borrowing money from other companies (Creditors).

Let’s say that you sell a product to a customer and they agree to pay you in 30 days time; this is known as a Debtor and is a use of your company’s money. A Creditor is the exact opposite of this; you receive products and agree to pay your supplier in 30 days time. The Debtor Creditor Ratio shows the relationship between these two amounts of money. Generally speaking, it makes good commercial sense to maintain a balance between these values so ideally they should at least cancel each other out. In any instance, to make your money work smarter, you always need to have more money in Creditors that you have in Debtors thereby showing a ratio of less than 1.0:1. Businesses begin to struggle and experience the effects of cash flow difficulties when this ratio is higher than 1.0:1.
Return On Sales

Net Profit ÷ Company Turnover (x 100)

Baseline: > 2.5%

This is the KPI that many franchise manufacturers refer to when discussing levels of profitability within their dealer networks and it is often referred to as the company’s Net Profit, or bottom line.

Example:
A) Net Profit = £2,178,099
B) Company Turnover = £62,914,213
C) Return On Sales % = 3.46% \( \frac{A}{B} \times 100 \)

This represents the bottom line profit of a company after all expenses have been deducted with the exception of taxation.

Although there is much talk at a high level about this Return On Sales, you cannot readily identify the causes for its upward or downward trends; you need to explore further up the structure of your management accounts.

This KPI is useful for budgeting and business planning purposes and for measuring the trends of your own performance over certain periods of time. However, it’s not much use when it comes to comparing your business with other businesses because no two businesses are funded in the same way. For instance, interest can be a sizable distortion; some businesses pay interest whilst others receive interest. If you wish to compare your business with other businesses a far better KPI to use to compare your performance is EBIT on page 325.
**Sales Retention Index**

**Profit After Breakeven ÷ Sales Dept Variable GP**

**Baseline:** >35%

This KPI is questioning the percentage of the Sales Department profit being retained after the Absorption Shortfall has been filled to reach the point of breakeven.

Example:

A) Direct Profit from Aftersales = £3,804,329  
B) Company Overheads = £4,590,595  
C) Sales Dept. Semi-Fixed = £687,101  
D) Total Overheads = £5,277,696 (B + C)  
E) Total Absorption = 72.08% (A÷D x 100)  
F) Absorption Shortfall = £1,473,367 (D - A)  
G) Sales Dept. Variable GP = £3,664,168  
H) Resorption = 40.21% (F÷G x 100)  
I) Profit After Breakeven = £2,190,801 (G - F)  
J) **Sales Retention Index** = **59.79%** (I÷G x 100)

The Sales Retention Index represents the flipside of Resorption and completes the circle on the inter-departmental relationships that converge to produce the overall company profits.

The Profit After Breakeven shown in the example above represents the residue after all of the company Overheads and expenses have been covered by the profits generated from both Sales and Aftersales. The only difference between this profit and the company Net Profit is the used vehicle trade activity. Therefore any profit or loss generated by the used vehicle trade activity should be applied to this figure to obtain the company Net Profit.
Service Absorption

Aftersales Direct Profit ÷ Business Overheads (x100)

Baseline: See Advanced Absorption on page xxx

This basic version of Absorption asks if the combined Direct Profits from Aftersales have the ability to cover (absorb) the cost of the company overheads.

Example:

A) Direct Profit from Aftersales = £3,804,329  
B) Company Overheads = £4,590,595  
C) Service Absorption = 82.87% (A ÷ B x 100)

Aftersales Direct Profit means the collective profits generated from all areas of the dealership with the exception of the Sales Department profit.

It doesn’t mean that Aftersales is more or less important than the Sales Department, it’s simply that Aftersales profitability is less volatile than the Sales Department profitability so it’s more stable for planning purposes in this scenario.

This example demonstrates that 82.87% of the company overheads are covered by Aftersales, which leaves the remaining 17.13% of the company overheads to be covered by the profits from the Sales Department.

This basic version only questions the company overheads, but if you need to assess company breakeven, you also have to consider other expenses; this is where the advanced version of Absorption takes over and is much more useful, see page 313.
Working Capital

Current Assets – Current Liabilities

Baseline: See Current Ratio

Working Capital is the value of money that is used to run your business on a day-to-day basis. It’s the money that’s invested within the part of your company where you buy and sell your products and services.

Example:
A) Current Assets = £5,883,860
B) Current Liabilities = £4,561,132
C) Working Capital = £1,322,728.31 (A - B)

This formula calculates the value of Working Capital within a business, but it doesn’t inform you of whether the value of Working Capital is sufficient to sustain the business on a day-to-day basis. This is the critical part because businesses don’t go bust because they run out of profit; they go bust because they run out of Working Capital.

If your business were a human body, then the Working Capital would be its blood. You need just the right amount to sustain life; too much and you might cause a haemorrhage, too little and you die.

If a business has too little Working Capital, it cannot survive and if it has too much, it can also be very damaging because it causes overage stock and poor credit control. To assess whether you have just the right amount of Working Capital for your business, you need to calculate Current Ratio, see page 322.
Acknowledgements

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**Personal**
My greatest desire has always been to give something back to the industry that has served me so well for the last 30 years and this above all is the absolute #1 reason for me writing this book; this is my contribution, my attempt to give something back. I hope you find as much enjoyment in reading it as I have found in writing it.

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*Thank you.*
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