

Automotive News

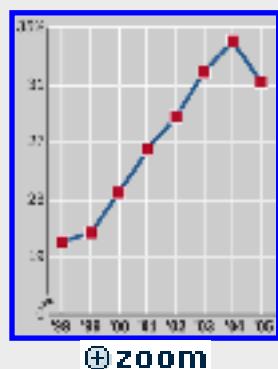
FINANCE & INSURANCE

New-vehicle service plan sales dip

Donna Harris | |

Automotive News | 6:00 am, June 12, 2006

At your service



Annual percentage of new-vehicle sales that included sales of service contracts

Source: NADA

The sales rate of new-vehicle service contracts fell last year for the first time since 1998, the National Automobile Dealers Association reports.

The typical new-car dealership sold service contracts to 31.2 percent of new-vehicle buyers in 2005, according to the 2006 edition of *NADA Data*. That penetration rate was down from 34.1 percent in 2004, when the rate neared its historic peak.

Industry analysts cite the growing U.S. market share of Asian automakers and an increase in vehicle leasing to explain the decline in service-contract business.

NADA analyst John Thomas notes Korean automakers offer factory new-vehicle warranties that are longer than the industry average. That reduces buyers' demand for extended service plans, he says.

Steve Hayes, COO of Aon Warranty Group in Glenview, Ill., says consumers tend to ascribe higher quality to vehicles built by Japanese automakers. That perception also lessens demand for service contracts, he says.

"Historically, the (service contract) penetration rates on those vehicles are not as good as on domestic vehicles because of the perceived quality," Hayes told *Automotive News*. "As the Japanese imports' market share increases significantly, the service contract penetration as a whole will go down a little bit."

Hayes adds, though, that Aon's sales of service plans have not fallen.

Industry consultants also say new-vehicle leasing is increasing. As interest rates climb, many auto lenders are shifting to lease promotions that help reduce monthly payments.

Leasing tends to curb demand for extended service plans, says Gil Van Over, a finance and insurance consultant in Chicago. Because lease terms tend to be shorter than vehicle ownership, leased cars and trucks are under warranty for most or all of the term, industry consultants note. Consumers are less likely to buy service plans for vehicles they don't own, consultants say.

The service contract penetration rate for new vehicles peaked at 35.0 percent in 1986, NADA says. Improvements in new-vehicle quality and wider factory warranty coverage eroded the sales rate until 1998.

That year, NADA says, the industry -- especially public dealership groups -- began to enhance sales training. Dealerships also improved consumer disclosures and introduced customer-friendly techniques to their F&I offices. The sales contract rate rose steadily from 1998 through 2004.

While the push for service contract business continues, "you are going to see slight fluctuations in penetration," says NADA's Thomas. "I would be concerned if it dropped again this year."

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